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### Budget Deficit Financing and Economic Stability in Nigeria

<sup>1</sup> Dominic Chukwudi Onoh, <sup>2</sup> George Duhu Isiwu, <sup>3</sup> Ogbonna Sabastine Nwali

<sup>1,2</sup> Department of Economics, Enugu State University of Science and Technology Business School, Nigeria

<sup>3</sup> Department of Entrepreneurial Studies, Enugu State University of Science and Technology Business School, Nigeria

Corresponding Author: **Dominic Chukwudi Onoh**

#### Abstract

Attainment of economic stability through budget deficit has remained the focal standpoint for the past successive governments in Nigeria. This paper empirically assessed the extent to which budget deficit financing has helped in economic stabilization in Nigeria. The study utilized time series data covering a span of 39 years (1985-2023). The data were obtained from diverse sources, including Central Bank of Nigeria (CBN), Budget Office of the Federation (BOF), National Bureau of Statistics (NBS), etc. The data include annual time series data on Gross Domestic Product (GDP), Government Budget Deficit (GBD), Inflation Rate (INF), Government Expenditure (GOVEXP), and External Debt (EXD). Method of evaluation include: Unit Root Test to examine stationarity of the variables, Augmented Dickey-fuller (ADF) to test for co-integration of the variables. Error Correction Method (ECM) was adopted to tie the short-run

dynamics of the co-integration to their long-run static dispositions. Vector Autoregressive (VAR) estimation methods were used to analyze the data. From the data analyses, the study found that deficit budget financing had a negative and significant influence on real gross domestic product (RGDP). The result of the estimation showed a negative and significant relationship between budget deficit and real GDP; as well as negative relationship between fiscal deficit and real GDP. In view of these, the paper recommended that budget financing in Nigeria should be focused on the productive sectors of the economy. Government should be economical with borrowing by having recourse to deficit financing only when it is extremely necessary; and fiscal discipline should be imbibed as a norm in both private and public lives of Nigerians to effectively nip unsustainable fiscal deficits in the bud.

**Keywords:** Budget Deficit Financing, Economic Stability

#### 1. Introduction

##### 1.1 Background of the Study

Attainment of Economic stability through budget deficit financing has remained the focal standpoint for the past successive governments of Nigeria. This is mainly because of the fact that economic stability measures the worth and viability of a country regionally and internationally. Theoretically, the development of budget deficit financing as an instrument for economic stability is often attributable to the Keynesian-expenditure led growth theory of the 1960s. After the economic depression experienced world over which affected most countries capacity to generate adequate revenue via taxation to finance economic development plans targeted at stabilizing the economy, most of these countries including Nigeria adopted Keynesian theory, which postulated that government has to induce the aggregate demand in order to stimulate economic growth and stabilize the economy since it cannot generate enough revenue to fund its development plans. Budget deficit financing occurred when a government in an attempt to stimulate and stabilize the economy spends more money than it receives as revenue, the difference being made up either by borrowing or minting new funds (Ways and Means). However, the implications of budget deficit financing on macroeconomic variables (inflation, employment, investment, Consumption) among others cannot be underestimated. An economy is taken to be stabilized when these variables are in a relatively stable condition. Economic Stability is the absence of excessive fluctuations in the macro-economy. An economy with fairly constant GDP/output growth, low unemployment rate and stable inflation would be considered economically stable. While an economy with frequent recessions, a pronounced business cycle fluctuation, price instability, huge national debt, exchange rate volatility, frequent financial crises would be considered economically unstable. Economic stability measures the economic prowess and competitiveness of a country with other countries of the world and it plays vital role in attracting both foreign and

domestic investment as well as influencing economic policies. The actualization of economic stability is the duty of every responsible government in any economic system irrespective of political arrangement. Economic Operators especially from the informal sector (Private Sector) are concerned about economic stability because it has direct impact on their performance. Gbosi (2002)<sup>[2]</sup> cited in Ojong and Hycent (2013) defined economic stability as the achievement of price stability, maintenance full employment and achievement sustained economic growth. This simply means that economic stability is desirable because it spurs economic growth that brings prosperity and employment. Shines (2014) postulates that economic stability in the economy shows no wide fluctuations in measures of economic performance, such as Gross Domestic Product (GDP). This suggests that stable economies demonstrate modest growth in GDP and employments while keeping inflation to a minimum acceptable level. Economists rely on multiple measures to ascertain the economic stability of an economy, these measures included national income, aggregate consumption, inflation, investment, international trade and finance for the measurement of economic stability of a country. Nevertheless, maintaining economic stability is partly a matter of introducing strategies aimed at avoiding economic crisis, low savings, high inflation and excessive volatility in exchange rates. In other words, economic instability can increase uncertainty, deter investment, inhibit economic growth and reduce standards of living of the citizen (Geoff, 2009). Meanwhile, in Nigeria, the value of budget deficits as a percentage of GDP declined to -0.1% in 1999. The share of budget deficits in total GDP has been declining from -2.0 % in 2003 to -1.1 % in 2005 and -0.6% in 2006. Nigeria recorded budget deficit equal to 1.80% of GDP in 2013 (Nigeria Budget Office of the Federation, 2014). Budget deficit averaged 2.10% of GDP from 2006 up till 2013, reaching an all-high of 4.6% of GDP in 2008 and recorded low of -6.6% of GDP in 2009 (Nigeria Budget Office of the Federation, 2014). Data on the consolidated federal government debt stock, as at December 2018 was 16.1% of GDP, in 2017 debt to GDP was 16.2%. CBN Annual Economic Report, (2018). This is vital because as mentioned earlier economic stability refers to the absence of excessive fluctuations in the macro-economy and an economy is considered economically stable when there is constant growth in the economy. Nigeria recorded a Government Debt to GDP of 38 percent of the country's Gross Domestic Product in 2022. Government Debt to GDP in Nigeria averaged 33.68 percent of GDP from 1990 until 2022, reaching an all time high of 75.00 percent of GDP in 1991 and a record low of 7.30 percent of GDP in 2008 (IMF, 2022).

### 1.2 Statement of the Problem

In Nigeria, budget deficit financing has taken the blame for most of the economic crisis that had affected its economic stability since 1980; over-indebtedness, high inflation, poor investment performance and low economic growth rate, among others. Attempt to regain stability at the macro level through fiscal adjustment achieved uneven success, raising questions about the macroeconomic consequences of budget deficits and fiscal deterioration in Nigeria (Udionye & Uma, 2013). It is on the basis of the above that Politicians and stakeholders of various ideologies argued that budget deficit reduction is critical to the future success of the Nigerian

economy. Although, many economists share the view that deficits are harmful, despite almost unanimous concern over budget deficits financing, there is considerable controversy about what effects does budget deficit financing has on stabilizing the economy of Nigeria. Again, unemployment, huge national debt and inflation have been an issue of concern, (all these are variables associated with budget deficit) to policymakers and researchers alike. This is mainly because unemployment, national debt and inflation are among key macroeconomics indicators and major determinant of economic stability of any economy. The Nigerian economy has remained largely underdeveloped despite the increases in size of budget deficit and economic growth rate recorded every year. In 2014 budget, Nigerian Economy was projected to grow at 4.5% and in 2015, it was projected to grow at 5.5%, a figure which is far higher than the developed country like USA that recorded the growth rate of 2.2% in 2014. The growth in Nigerian economy has been described as exclusive growth which is worrisome and calls for concern. The per capita income is low, unemployment and inflation rates are high, there are many socioeconomic challenges. The various macroeconomic policies implemented by the government have been unable to achieve desired goals of price stability, reduction in unemployment and sustainable output growth. It is against these backdrops; that this study will investigate the relationship between budget deficit financing and economic stability in Nigeria.

### 1.3 Objectives of the Study

The broad objective of the study is to analyse budget deficit financing and Economic Stability in Nigeria. The specific objectives are to:

1. Investigate the impact of budget deficit financing on economic stability in Nigeria.
2. Examine the impact of government expenditure and external debt on economic stability in Nigeria.
3. Ascertain the causality relationship between the budget deficit, government expenditure, external debt and economic stability in Nigeria.

### 1.4 Significance of the Study

This study is beneficial and relevant to government, policy-makers, stakeholders and researchers. The result of this study would help government with an insight on how Budget Deficit Financing are maximized towards stabilizing and growing the economy of Nigeria.

Policy decisions on future borrowing will be made based on the recommendation of this study especially in terms of how to utilize budget deficit to achieve macroeconomic objectives like reducing unemployment, balance of payments, price stability, and sustainable economic growth. The outcome of this study will be useful to researchers by adding to the body knowledge and to the existing literature and serve as a source of reference for future research by students as well as researchers wishing to conduct further research in this area.

## 2 Literature Review

### 2.1 Conceptual Review

#### 2.1.1 Budget Deficit.

Government faces budget deficit whenever it's expected revenue falls short of it's expected expenditures. In other to realize the funds necessary to cover the gap / deficit,

Government must borrow either from internal or external sources or resort to Ways and Means. Budget deficit finance is an economic state in which government spending is more than its earning. It is when the expected government expenditure outweighs the anticipated government revenue within a fiscal year (Obadan, 2011). Anyanwu (1997) explained budget deficit to mean a situation where government expenditure exceeds government revenue over a given period of time. When a deficit is involved, it is important to find remedy for financing such deficit to avoid its negative consequences. In Nigeria, fiscal deficits have been blamed for most of the economic instability that bedeviled the country for about decades resulting in heavy indebtedness, high inflation, poor investment performance and growth (Ezeabasili, Mojekwu & Herbert, 2012). In words of Nayab (2015), a budget deficit is the surplus of public sector spending over revenues.

### 2.1.2 Economic Stability

Economic stability is a state in which macroeconomic conditions of a country are relatively stable and healthy. This state can be achieved by implementing sound monetary and fiscal policy reforms aimed at countering the adverse effect of fluctuations in business cycles. Economic stabilization is instrumental to economic growth as it attracts the necessary capital and productive resources required for growing the economy. CBN (2016). Economic stability refers to an absence of excessive fluctuations in the macro-economy. An economy with fairly constant output growth and low or stable inflation would be considered stable. Economic stability is a term that has been in focus for the past years now mainly because of the economic downturn experienced globally. Many share markets plunged and business plummeted, which gave rise to one of worst economic crisis witnessed by this present generation. In fact, Economic stability describes the state where an economy is free from various factors disrupting its smooth functioning and growth. The variables affecting stability include inflation, recession, policy changes, global market, and fiscal deficits as well as political situation (Nanditha Saravanakumar (2024).

## 2.2 Theoretical Literature

For the purposes of this work the theoretical frameworks that were considered relevant are as follows: Keynesian economic theory, Neoclassical economic theory, Ricardian equivalence approach.

### 2.2.1 Keynesian Economic Theory

This Keynesian Economic Theory was developed by a British Economist John Maynard Keynes (1936)<sup>[4]</sup>. The Theory was previously used by Ali (2014); Bakare, Adesanya and Bolarinwa, (2014); Muhammad, Sofia, Syed and Abbas, (2014); Okelo, Momanyi, Lucas and Alia, (2013); Okro, (2013); Ojong and Hycenth (2013) in their respective studies. Keynesian theory states that public expenditures can contribute positively to economic growth by increasing consumption through increase in employment, profitability and investment. The Central tenet of this school of thought is that Government intervention can stabilize the economy, Sarwat Jahan, Ahmed Saber Mahmud, and Chris Papageorgeou, (2014). The Theory further states that government can reverse economic downturns by borrowing from the private sector and returning the money to private sector through various spending programmes. It explained

that effective government intervention in the market through budget deficit financing was the only method of ensuring economic growth and stability. He added that through efficiency in resource allocation, regulation of markets, that stabilization of the economy and harmonization of social conflicts will be achieved. Keynes stated that in the short run, economic growth and stability is strongly influenced by total spending in the economy. The theory regards the economy as being inherently unstable and required effective government intervention through spending to achieve economic stability.

In another view, Okpanachi and Abimiku, (2007) opined that budget deficit stimulates economic activities in the short run by making households feel wealthier and hence, raising total private and public consumption expenditure. This means that Keynesian theory causes money demand to rise and interest rate will also increase which will make investment to decline. Keynesian school of thought often argue that private sector decisions lead to inefficient macroeconomic outcomes which require effective policy responses by the public sector, in particular, monetary policy actions by the Central Bank of Nigeria and Fiscal policy measure by the Federal Ministry of Finance, in order to stabilize output in the economy.

### 2.2.2 Ricardian Equivalence

The Ricardian Equivalence Hypothesis, postulated by David Ricardo and completed by Barro (1989). The Ricardian equivalence explained the use of debt or taxes to meet financing needs of the government. It states that if people know that using debt today will translate to more taxes in the future, then there is no difference in using debt or taxes. This suggested that the use of debt is the same as taxes. It posited that budget deficits has no effect on the economy. This is mainly because an increase in budget deficits will be repaid either now or in future since a cut in taxes today must be matched by future increase in taxes thereby leaving real rate of interest, private investment, exchange rate and domestic production unaffected (Awolaja & Esefo, 2020).

The theory is based two assumptions which are the assumption of rational expectations and household taxation which opined that as budget deficit increases through borrowing, and as taxes reduce, the government will not increase future taxes to repay the interests. Also they postulated that people found out by previous experiences that increase in government bond as a result of decrease in taxes offers temporary revenue for the individual at the present time, and as the debt of government continues to rise, people will save more so as to provide higher tax paying in the future.

The theory thus opined that government budget deficits do not influence aggregate demand in an economy during a given period. The underlying philosophy of Ricardian school of thoughts can be that Funds required for financing government programmes may be raised by collecting taxes or borrowing. Undoubtedly, government is obliged to repay the sum borrowed today or later by raising taxes above expected present value. The valid option becomes either tax now or tax later. Assuming Government overspends more than budgeted by means of deficit financing (it means that government will tax later), The Ricardian school of thought maintained that though taxpayers will hold more money now, they should be aware of their duty to pay more tax in

future, thus should save now to meet that more tax obligation as at when due.

### 2.3 Empirical Literature

Akinmulegun (2014)<sup>[16]</sup> in his study of deficit financing and its effect on economic growth in Nigeria employing the econometric technique of Vector Auto Regression (VAR) model. The variables used in the study are as follows: Real Gross Domestic Product (RGDP), the Gross Capital Formation (GCF), the real interest rate (RINTR), Inflation rate (INFR) and budget deficit. It was discovered that deficit financing has not contributed significantly to economic growth in Nigeria. This is attributed to the negative impact of deficit financing on economic growth during the period under review. The study thus recommended that going forward government should reduce unnecessary public spending, ensure greater budget discipline and adopt a financial structural transformation that can help to reduce wastage in public spending.

Adeleke and Abdulsalam (2016) examined the impact of Budget deficit on Nigeria's economic growth from 1983 – 2014. Ordinary Least Square (OLS) method of regression analysis was employed to determine the long-run relationship among variables. The ADF result showed that all the variables were stationary and co-integrated. It equally showed that there is a significant relationship between the deficit budget and inflation as well as money supply and inflation. They therefore recommended that government should display a high sense of transparency in fiscal operations to bring about realistic fiscal deficit.

Sanya and Lawal (2016) investigated the impact of fiscal deficit on the growth of Nigeria economy using co-integration and error correction model, their result showed that there exists a stable long-run relationship between economic growth and budgeting components (current and capital expenditure). They equally argued that deficit budget is one of the indicators of macroeconomic instability and significantly discourage human capital accumulation.

Kurantin (2017) utilized a panel data set between 1994 and 2014 to examine the effects of budget deficit on economic growth in Ghana. The study evaluates the Ghana experience on fiscal deficit and its implications on sustainable growth and development. Using an OLS technique to run the estimation, findings revealed that budget deficit has a negative effect on economic growth while investment shows a positive impact on economic growth.

Liu, Hsu and Younis (2008) carried out a study on the association between Government Expenditure and Economic Growth: The Granger causality test on US Federal government data, from 1947 - 2002. Aggregate data and disaggregate data with the sub-categories of five federal expenditures, including, defence, human resources expenditure, physical resources expenditure, net interest payment and other expenditure. The result of the study suggests that total federal government expenditure is more consistent with Keynesian's theory while there are diversified causal relationships among five sub-category of federal expenditure. The policy recommendation included that the US federal government should invest more public resources in human resources expenditure under the assumption that economic growth is the utmost important item on the government Agenda.

Ubi and Inyang (2018) ascertained fiscal deficit and its implication of economic development in Nigeria. The study

noted two phenomena based on the time series data. (1) That in 37 years (1980 - 2016), the country's fiscal performance ended in deficits and had surplus for only two years. (2) The rising fiscal deficit recorded more or recurrent expenditure than capital expenditure. Unfortunately, the lopsided style of spending was actually seen as incapable of stimulating economic development in the long run. Specifically, the study assessed the effect of fiscal deficit on selected macroeconomic variables which included gross domestic product, unemployment, inflation, per capita income and balance of payment. The findings proved that fiscal deficit influenced growth of per capita income, economic growth as well as BOP stabilization, while fiscal deficit did not reduce inflation and unemployment rates over the period.

Nwaeze (2017) ascertained the relationship between fiscal deficits and macroeconomic stability in Nigeria from 1970 to 2016. Data was sourced from Central Bank of Nigeria statistical bulletin. The study utilized inflation rate (INFL) and Exchange rate (EXCR) to proxy Macroeconomic stability whereas overall fiscal deficits (OFDE), fiscal deficit financed by domestic borrowing (DBFD), fiscal Deficit financed by external borrowing (EBFD), interest rate (INTR), money supply (MS), foreign direct investment (FDI) and external reserve balance (EXTR) were used as the independent variables. The study employed descriptive statistics, unit root test, co-integration and vector autoregressive (VAR) estimation methods to analyze the data. The results of the variance decomposition showed that interest rate (INTR), overall fiscal deficits (OFDE), and the size of fiscal deficits financed by domestic borrowing (DBFD) were the main shocks causing the variation in Inflation (INFL), while overall fiscal deficits (OFDE), the size of fiscal deficits financed by domestic borrowing (DBFD) were the main shocks causing the variation in exchange rate (EXCR) in Nigeria. The study therefore recommended that fiscal deficits should be moderated and financed mainly via bonds as empirical findings suggested that both domestic and external borrowing options were detrimental to the macroeconomic stability of the Nigerian economy within the period of the study.

Moses, Tule & Usman Nurudeen & Olorunfoba & Apinran, (2019) experimenting fiscal theory of price level in Nigeria. in study of the Efficacy of Fiscal Theory of Price Level in Nigeria using an Auto Regressive Distributive lag (ARDL) model for the period from 2002 - 2017. Testing that price level is not independently determined by the monetary authorities, rather it is as a result of the relationship between monetary and fiscal authorities. The result show that fiscal deficits have a positive and statistically significant effect on inflation in all models estimated.

### 3. Methodology

This work made use of Ex-Post facto research design which enables us to measure the effect or relationship between dependence variable and explanatory variables using time-series secondary data. The data were collected from diverse sources, including Central Bank of Nigeria (CBN) Statistical Bulletin, Budget Office of the Federation (BOF), National Bureau of Statistics from year (1985 - 2023). To empirically examine the impact of budget deficit financing on economic stability in Nigeria, the researcher subjected the data collected to Augmented Dickey-Fuller Unit Root test statistic, Johansen Co-integration test, Breusch- Godfrey serial Correlation LM Test, Heteroskedasticity Test



(Breusch-Pagan-Godfrey) and Ramsey Reset.

### 3.1 Theoretical Framework

The study anchored on the Keynesian aggregate demand framework. In a simple Keynesian framework, the desired aggregate demand relationship in the Keynesian framework is expressed as follows:

$$Y = C + I + G + (X - M) \tag{Eqn 3.2.1}$$

The behavioural equation is written as;

$$\begin{aligned} C &= a + bY^d, & b > 0 \\ Y^d &= Y - T \\ I &= \theta + Y_i, & Y < 0 \\ G &= G^* \\ X &= S + \sigma e, & \sigma > 0 \\ M &= M + \phi Y^d, & \phi > 0 \end{aligned}$$

Where Y = output, C = Consumption, = Disposable income, T = Tax revenue, I = Investment,  $\theta$  = exogenous investments, I = interest G = exogenous government expenditure (G\*), X = exports, s= exogenous exports, e=exchange M= Imports, m= exogenous imports and b,  $\sigma$ ,  $\phi$  and  $\gamma$  are coefficients.

### 3.2 Model Specification

This study specifically adopted the model of Emefiele, Obim and Ita (2019) that how financial and stability can aid foreign direct investment inflow. The study showed that government deficit budget was taken as a function of s Domestic Product (GDP). The model is therefore estimated as follows:

$$Y_t = \beta_0 + \beta_1 X_t + U_t$$

The functional form of the model

$$GDP = F(GBD, INFR, GOVEXP) \tag{1}$$

Where:

- GDP = Gross Domestic Product (Dependent Variable)
- GBD = Government Budget Deficit (Independent Variable)
- INF = Inflation rate (Explanatory Variable)
- GOVEXP = Government Expenditure (Explanatory Variable)

However, the model has been modified to incorporate External Debt as one of the explanatory or independent variables and the preferred model should read in the following functional forms:

$$RGDP = F(GDB, INFR, GEX, EXD) \tag{2}$$

$$RGDP_t = \beta_0 + \beta_1 BDF_t + \beta_2 INFR_t + \beta_3 GEX_t + \beta_4 EXD_t + U_t \tag{3}$$

Where:  $RGDP_t$  = Real Gross Domestic Product of Nigeria, which measures economic stability and growth within the period of the study.

$GDB_t$  = Government Budget Deficit for the period of the study

$INFL_t$  = Inflation rate for the period of the study

$GOV EXP_t$  = Government expenditure for the period of the study

$EXD_t$  = External Debt for the period of the study

T = the time period chosen for the study (1985 - 2023)

$\beta$  = Constant term  $\beta_0, \beta_1, \beta_2, \beta_3,$  and  $\beta_4$  = the slope of the independent and explanatory variables

$U_t$  = Error term which covers other variables not captured in the model.

## 4. Data Presentation and Analysis

**Table 1:** Augmented Dickey Fuller (ADF) Unit Root Test Result

Variables	ADF Statistics (1 <sup>st</sup> Difference)	5% Critical Value	Probability Value (P-Value)	Order of Integration
RGDP	-7.437559	-2.951125	0.0000	1(1)
GDB	-5.624031	-2.971853	0.0001	1(1)
GOV EXP	-4.342310	-2.951125	0.0016	1(0)
INFL	-4.514653	-2.960411	0.0011	1(1)
EXD	-4.334567	-2.951125	0.0016	1(1)

Source: Authors Computation, 2024

The result of the unit root test in the table above shows that the variables are stationary at same orders of integration except one (GOV EXP). Each of the variables has unit root, and attained stationary after first differencing (i.e 1 (1)) except One. That is to say that RGDP, GDB, INFL, were stationary at first difference with intercept at 5% level of significance that is they all became stationary at first difference. However, government expenditure was to be stationary at level. But since the results exhibit stationary at first differencing, it is imperative to carry out co-integration test to ascertain whether the variables have long-run equilibrium relationship in the model by using the Johansen Co-integration test.

**Table 2:** Results of the ARDL Bound TEST

F-Statistic	Critical Value		
	Significance	Lower Bounds 1(0)	Upper Bounds 1(1)
4.667756	5%	2.86	4.01
	10%	2.45	3.52

Source: Authors Computation, 2024

The null hypothesis of the ARDL bound test is that there is no long relationship (co-integration) between the variables. Given that the computed F-Statistic (4.7) of the ARDL bounds test is greater than the upper critical value (4.01) at 5% level of significance, the null hypothesis is rejected. This signifies that there is co-integration among growth in real GDP as the dependent variable and the independent variables. Hence, we can estimate the short and long run effects of the independent variables on the dependent variable. The result of the long run effects of government expenditure, external Debt, government budget deficit and inflation rate on GDP are presented below in the table below:

**Table 3:** Long run estimates of the ARDL Model

Variable	Coefficient	Std error	T-Statistics	Probability
GOV EXP	1.604186	0.424166	3.781978	0.0026
GBD	-1.234723	0.960713	-1.285215	0.2230
EXD	1.043279	0.708587	1.472338	0.1667
INF	1.487268	1.005751	1.478764	0.1650
C	-15.387226	16.592931	-0.927336	0.3720

Source: Authors Computation, 2024

From the results of the long run estimated co-efficient and using the lag length of (1,3,3,4,4), the results indicated that only government expenditure is statistically significant and the coefficient has a positive sign. The results also showed that holding other variables constant, a 1% increase in government expenditure will yield a 1.6% increase in real GDP. On the other hand, if all things remain the same, a 1% rise in government deficit budget would cause a reduction in real GDP equal to 1.71. That is a negative and weak relationship exists between government deficit budget and real GDP. This result disqualified the a priori expectation of a positive relationship between government deficit budget and real GDP. Inflation rate and External Debt revealed a positive and insignificant relationship with real GDP, contrary to the expected sign of positive and negative signs respectively. The value of the intercept (-15.4) which is the predicted value of real GDP assuming all the independent variables are equal to zero and is statistically significant at 5% level.

**Table 4:** Results of the Short Run Estimation

Variable	Coefficient	Std. Error	t-statistics	Prob
GOV EXP	-3.205640	1.505861	-2.128776	0.0547
GBD	0.037036	0.082766	0.447478	0.6625
EXD	-0.031002	0.621835	-0.049855	0.9611
INF	-0.005787	0.274486	-0.021083	0.9835
CoInt Eq (-1)	-0.634538	0.296541	-2.139802	0.0436

ARDL model econometrics criteria: R-Squared=0.974588; Adjusted R-Squared =0.934353; F-statistic=24.22221; Prob(F-statistic)=0.000000

Source: Authors Computation, 2024

From the above Table 4 the elasticities of the output with respect to the independent variables in the short run showed that one variable Gov EXP is statistically significant while government budget deficit (GBD), External Debt (EXD), and inflation rate were found to be insignificant. Meaning that GBD, EXD, and INF do not contribute to economic stability and growth. Nonetheless, the coefficient of the error correction term (ECT) is significant and it has the correct signs. This supports the finding of a stable long run relationship among the variables. In addition, the results of the short-run estimates show that government expenditure (GovEXP) and Inflation (INF) halt economic stability and growth in Nigeria and statistically insignificant at the 5% level. While government Budget Deficit (GBD) indicated positive insignificant relationships with economic stability and growth. The R<sup>2</sup> that is the coefficient of determination, showed that 97% of the total variation in the dependent variable (economic stability/GDP), can be explained by the independent and explanatory variables while only 3% cannot be explained but is captured by the error term. The drop to about 93% after adjust for degree of freedom is still significant. The F-statistic is approximately 24.22 with probability of 0.000000. The significance of this value implies that the data used in the estimation fitted well into the regression equation, thus the model is adequate in explaining the impact relationship of the independent variables on real GDP in Nigeria. R<sup>2</sup> is the summary measure that explains how well the sample regression line fits the data.

**4.1 Granger Causality Test**

Given that this study is basically an impact study, Granger

Causality Test Result, among other things, enable us ascertain both the direction and magnitude of effect between the dependent variable and the independent variables. In order to achieve this objective, the Granger Causality Test was resorted to.

**Table 5:** Granger Causality Test Result

Null Hypothesis	Obs	F-statistics	Prob	Decision
GBD does not Granger Cause RGDP	34	2.90074	0.0711	GBD → RGDP unidirectional causality
RGDP does not Granger Cause GBD		6.95102	0.0034	
GovEXP does not Granger Cause RGDP	34	2.06830	0.1446	GovEXP→RGDP unidirectional causality
RGDP does not Granger cause GovEXP		3.98492	0.0296	
EXD does not Granger Cause RGDP	34	2.90074	0.0711	EXD → RGDP unidirectional causality
RGDP does not Granger cause EXD		6.95102	0.0034	
INF does not Granger Cause RGDP	34	1.10995	0.3432	INF → RGDP unidirectional causality
RGDP does not Granger Cause INF		4.51395	0.0196	

Source: Authors Computation, 2024

The causal relationship between RGDP, GovExp, EXD, GBD, and INF, is the main focus of this empirical investigation. The Pairwise Granger test helps to determine the direction of causality between the variables in the specified model. The result from Table 5 showed that the p-value of GBD and RGDP are 0.0711 and 0.0034 respectively. The probability is less than 0.05 we therefore reject the null hypothesis and accept the alternative hypothesis. Meaning there is an unidirectional causal relationship between GBD and RGDP and the direction of causality is from RGDP to GBD. The table also showed that there is unidirectional relationship between Gov Exp and RGDP within the period of the study. As well there is unidirectional relationship between INF and RGDP and the direction of causality is from RGDP to INF. EXD and RGDP also showed a unidirectional relationship with each other running from real GDP to inflation.

**4.2 Test of Hypothesis**

The test of three hypotheses are presented in this section. They are represented as follows:

**4.2.1 Test of Hypothesis One**

**H0<sub>1</sub>:** Budget deficit financing has no significant impact on economic stability in Nigeria.

Referring to the first hypothesis which states that Budget deficit financing has no significant impact on economic stability in Nigeria, the study uses the estimated results in Table 3. As shown in the table, the p-value government deficit financing (GBD) is 0.2230. This is substantially higher than the critical value of 0.05. Thus we accept the null hypothesis. Accepting the null hypothesis implies that budget deficit financing has no significant impact on economic stability in Nigeria.

### 4.2.2 Test of Hypothesis Two

**H0<sub>2</sub>:** External debt and government expenditure have no impact on economic stability in Nigeria.

Referring to the second hypothesis which states that External debt and government expenditure have no impact on economic stability in Nigeria, the study uses the estimated results in Table 3. As shown in the table, the p-value for external debt and government expenditure are 0.1667 and 0.0026 respectively. This implies that external debt is substantially higher than the critical value of 0.05 while government expenditure is less than the critical value of 0.05. Thus, we accept the null hypothesis of external debt and reject the null hypothesis of government expenditure. This implies that external debt has no impact on economic stability in Nigeria; while government expenditure has impact on economic stability in Nigeria.

### 4.2.3 Test of Hypothesis Three

**H0<sub>3</sub>:** There is no causality relationship between budget deficit, government expenditure, external debt and economic stability in Nigeria.

The causal relationship between RGDP, GovExp, EXD, GBD, and INF, is the main focus of this empirical investigation. The Pairwise Granger test helps to determine the direction of causality between the variables in the specified model. The result from Table 5 the Pairwise Granger test showed that the p-value of GBD and RGDP are 0.0711 and 0.0034 respectively. The probability is less than 0.05 we therefore reject the null hypothesis and accept the alternative hypothesis. Meaning there is an unidirectional causal relationship between GBD and RGDP and the direction of causality is from RGDP to GBD. The table also showed that there is unidirectional relationship between Gov Exp and RGDP within the period of the study. As well there is unidirectional relationship between INF and RGDP and the direction of causality is from RGDP to INF. EXD and RGDP also showed a unidirectional relationship with each other running from real GDP to inflation.

**Table 6:** Summary of results of the Post Diagnostic Tests

Diagnostic Tests		
Test	F-Statistic	Probability
Breusch- Godfrey serial Correlation LM Test	1.657001	0.2390
Heteroskedasticity Test: Breusch-Pagan-Godfrey	0.401420	0.9634
Ramsey Reset Test	1.702509	0.2186

**Source:** Author Computation, 2024

For a proper interpretation of results, the results of the ARDL co-integration test was interpreted and evaluated for serial correlation, heteroskedasticity and stability. In Table 6 above it can be observed that the probability values for Breusch-Godfrey serial correlation LM Test and Breusch-Pagan-Godfrey Heterskedasticity Test are greater than 0.05, thus the null hypothesis of no serial correlation and heteroskedasticity were not rejected. Also, the probability of value (0.22) of the Ramsey Reset Test for stability is greater than 0.05 hence we failed to reject the null hypothesis that the model is correctly specified.

## 5. Summary of Findings

Finding arising from this study can be summarized as follows:

1. External source of deficit budget financing had a negative and significant influence on real gross domestic product (RGDP). It contributes significantly to the economic stability in Nigeria, especially over the period covering 1985 - 2022 as explained by the negative coefficient value (-0.031) of the explanatory value (EXD), as well as the corresponding probability value of the t-statistic (-0.0498) for EXD which is less than 0.05 critical value.
2. Budget Deficit plays an important and increasing role in achieving full employment, sustainable economic growth, price stability and poverty reduction. Theoretically both Keynesian and neoclassical economists provided tools for government intervention especially with regards to government budget deficit financing. The result of the estimation showed a negative and insignificant relationship between budget deficit and real GDP. This shows that fiscal deficits are the total debt generated by the government to finance its expenditure, indicating that government has no other option than borrowing. When fiscal deficit is high, it implies that government has to borrow heavily, meaning demand for loan will rise in the market leading to higher interest rate and high cost of borrowing. Private investors are crowded out thus existing project stalled.
3. The finding equally shows there negative relationship between fiscal deficit and Real GDP. This is theoretically underpinned by the neo-classical school of thought. This study is line with the studies by Mahauty (2012) and Kurantin (2012) they found a negative but significant relationship between fiscal deficit and GDP/Economic growth. However this result was in contrast to the one conducted by Okoye and Akenbor (2010) they found that deficit financing has a positive and significant impact on economic activities and stability in Nigeria. The study findings also showed that there was a unidirectional causal relationship between government deficit budget and economic stability.
4. The finding also posits that a 1% increase in government expenditure will yield a 1.6% increase in Real GDP. Meaning that there was a positive and significant relationship between real GDP and government expenditure. Thus there was a unidirectional causal relationship from real GDP to government expenditure during the period under review. This was in line with the study by Liu, Hsu, and Younis (2008) who found that GDP causes growth of government expenditure. On the other hand growth of real GDP causes expansion of government expenditure. The error correction term in the model is highly significant and correctly signed. Specifically, the result indicates a coefficient of (-0.63 with a P value of (0.04), which is less than (0.05) level of significance. The results of ECM indicate that there is system adjustment from the short disequilibrium to the long-run equilibrium. The coefficient is -0.63 meaning that system corrects its previous period disequilibrium at a speed of 63% yearly.

## 5.1 Conclusion

Deficit Budget Financing has been broadly examined theoretically and empirically. The concept of allowing government expenditure to exceed its income with a view to improving economic activity and lowering unemployment is affirmed world over. In line with empirical ideologies, Ordinary Least Square (OLS) economic technique was adopted to evaluate Budget Deficit Financing and Economic Stability in Nigeria. However with real GDP proxied economic stability as the dependent Variable while GBD Government Budget Deficit (Independent Variable), Inflation rate (INF, Explanatory Variable), Government Expenditure (GOVEXP, Explanatory Variable) and thereafter External Debt EXD as explanatory variable. Preliminary tests of presence of unit root and normality were conducted using Augmented Dickey-Fuller (ADF) and descriptive statistics respectively. While the former affirmed the stationarity traits of the variables, the latter confirmed that the series were normally distributed.

## 5.2 Recommendations

1. Budget Deficit financing in Nigeria should be focused on the productive sectors of the economy. This is so because budget deficit financing is yet to bring about the much-needed economic turnaround, as a result, tested result-oriented policies are needed to achieve economic breakthrough in Nigeria. This can be achieved by diversification of the economy away from oil. This can also be done by borrowing for profitable self-financing investment projects.
2. Government should be economical with borrowing by having a recourse to deficit financing only when it is extremely necessary to do so. Borrowing is not bad but what is bad is the mismanagement and misapplication of borrowed fund. This is because borrowing to address fiscal deficit increases money supply in a way. Government should adopt fiscal adjustment mechanism that enhances income generation through improved taxes and expansion fiscal space rather than borrowing to finance deficit year in year out.
3. Fiscal discipline should be imbibed as a norm in both private and public lives of Nigerians to effectively nip unsustainable fiscal deficits in the bud. Government of Nigeria at all level should promote fiscal discipleness in governance and eradicate wastage in public expenditure. Policy makers should endeavour to focus on maintaining inflation rate at low or minimal level (single digit) and as well ensure that interest rate is stabilized.

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