Openness and the Effects of Fiscal and Monetary Policies on Real Output in Nigeria (1960-2003)

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ABSTRACT

The study examined the effects of monetary and fiscal policies on the real output growth in the small open Nigerian economy. Specifically, it verified the implication of increasing economic openness on the efficacy of monetary and fiscal policy and also established whether fiscal and monetary policies had symmetrical effects on real output in Nigeria. This was with a view to establishing the validity of macroeconomic policy ineffectiveness proposition of new classical school in Nigeria.

The study used annual secondary time series data from 1960 to 2003 on Nigeria, collected from International Financial Statistics (IFS) Yearbook published by International Monetary Fund (IMF), 1990 and 2003 editions. A modified Generalized Autoregressive Consistent Heteroskedastic (GARCH) model and Vector Error Correction Mechanism (VECM) technique were used to generate the anticipated and unanticipated series used for estimating an open economy version of the new classical macroeconomic model. Two measures of fiscal and monetary shocks were combined with openness and real oil price shocks in a VECM model to assess the effects of anticipated and unanticipated policy shocks on the output equations and to draw policy inferences

The empirical results showed that anticipated and unanticipated fiscal and monetary shocks had no significant positive effects on real output. Furthermore, the degree of openness and oil price shocks {with coefficients -0.434 (t-value -2.08,$p < 0.05$) and -0.684 (t-value -2.11,$p<0.05$)} had negative implication on the efficacy of macroeconomic policy in Nigeria. Thus, a 10% increase in fiscal and monetary policies in the presence of increasing economic openness and oil price shocks would cause more than 4.34% and 6.84% reduction in real output respectively. In addition, the results showed that both expansionary and contractionary policy shocks had adverse negative effects on real output growth. Specifically, while expansionary policy shocks had negative {–1.50(t-value -3.76, $p<0.05$)} as against the expected positive effects, the contractionary policy shocks had no significant negative {0.01 (t-value -0.03,$p>0.05$)} effects on real output in Nigeria. Similarly, the impulse responses and variance decomposition analysis also established that monetary and fiscal policies played little causal role in explaining real output fluctuations in Nigeria.

The conclusion that emerged from the results was that the open macroeconomic version of policy ineffectiveness proposition was valid with respect to fiscal and monetary policy shocks in Nigeria. This is in consonance with earlier works in this area on other countries. Similarly, the result was in agreement with the Dutch Disease Syndrome and also confirmed that policy asymmetry was a Nigerian phenomenon.