2020

REPORT OF THE

OYOSTATE DEBT SUSTAINABILITY ANALYSIS

(S-DSA)

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OYO State Technical Team

CHAPTER ONE

1. Introduction

1.1 The Oyo State 2020 Debt Sustainability Analysis Report was formulated so that the State's public debt is sustainable. This report analyses trends and patterns in the State's Public finances during the period 2015-2019, and evaluates the debt sustainability in 2020- 2029. This analysis highlights recent trends in revenue, expenditure, and public debt, and the related polices adopted by the State Government. This will ensure that the State is able to service its debt in the short, medium and long-run without renegotiating or defaulting, and without having to undertake policy adjustments that are implausibly large from an economic and political standpoint. A sustainable debt provides confidence that the government will be able to borrow and pay potential creditors. Unsustainable debt levels, on the other hand, present risks to government expenditures on development and social programmes since a large proportion of revenue would be diverted to debt service.

Given the State's own forecasts for the economy and reasonable assumptions concerning the States revenue and expenditure polices going forward, the long-term outlook for the public debt appears sustainable. The State exhibits a solid debt position that appears sustainable in the long term. A solid debt position result from the State's strong performance in terms of improving Internally Generated Revenue (IGR) underpinned by the increase in the Tax net of the State Government particularly from the informal sector.

The S-DSA was conducted between November and December, 2020 using the 5 years historical data from 2015 – 2020 on the State revenue, the expenditure and debt stock. The participating Agencies include;

i. Ministry of Finance;

ii. Ministry of Budget and Economic Planning;

iii. Board of Internal Revenue Services; and

iv. Accountant General Office

CHAPTER TWO

OYO STATE FISCAL AND DEBT FRAMEWORK

2.1 The State fiscal reforms essentially focus on expanding the Internally-Generated Revenue and reducing debt stock and liability. Specifically, the State has carried out a number of strategic reforms in the areas of restructuring and strengthening of Revenue Generating Institutions, Amendment of Debt Management Agency's Law and Development of Domestic Arrears Clearance Framework, Adoption of Treasury Single Account (TSA) and IPSAS cash basis and accrual methods, Automation of Payroll System and Public Procurement reforms as well as Alternative Project Funding Approach- Contractor's financing method among others. Furthermore, the State is on the verge of having her Development Plan, Investment Plan and Pensions system reforms through the adoption of the Contributory Pension Scheme.

2.2 The Year 2020 budget was derived from Oyo State Accelerated Development Road Map put in place by the present administration and the State is currently preparing Development Plan document together with Medium-Term Expenditure Framework (MTEF). The main effect of Covid- 19 on the initial year 2020 budget was the amendment of the budget which enables the State Government to prioritize her finances in Agriculture, Health, Education and Security as a catalyst for the exponential growth of the State's economy.

The Covid-19 pandemic redirected the focus of Year 2020 budget which culminated into downward review of the budget size from N213billion to N174billion. Capital Expenditure decreased from N103.36B in the original Budget to N64.29b while Overhead Cost was reduced from N31.16B in Approved Budget to N30.94b. Similarly, there was a decrease in C.R.F.C. from N40.86B in the original Approved Budget to N34.51b. However, the Personnel Cost increased from N38.45b from original Approved to N39.52b in the reviewed Budget to accommodate payment of the minimum wage and employment of additional medical staff.

The State IGR initially budgeted at N62.64 billion was reviewed downward to N53.56 billion in the revised budget. This downward review was occasioned by the lockdown caused by COVID-19 during which businesses and other sources of IGR were affected especially in the Q2 and Q3.

Based on the revised 2020 Budget, more than 15% of the budget was provided for funding of COVID-19 related activities.

2.3 The State does not have Medium-Term Debt Management Strategy but efforts are being put in place to ensure that it is developed before the end of 2021.

CHAPTER THREE

3.0 **REVENUE, EXPENDITURE AND PUBLIC DEBT TREND (2015 – 2019)**

3.1 The revenue profile of the state was on upward trajectory from Year 2015 to Year 2019. The increase in revenue in the period under review resulted into enhanced nominal growth rate of 74.42%. IGR, grants, FAAC and other FAAC transfers rose geometrically on yearly basis up till 2019. There was also sharp increase in expenditure of the state. The major cause of the increased expenditure is the personnel cost which consist of salary, pensions and other public and civil servants' social benefits. This was due to implementation of new minimum wages, payments of salaries and pension arrears and new recruitment carried by the state government. The variation of total revenue as a percentage of state GDP stood at (15) threshold.

3.1.1 Revenue Performance.

The revenue trend was on marginal increase from Year 2015 to 2016 until 2017 when it increased geometrically from N70.383 Billion in 2016 to N114.910 Billion in 2017. However, there was a sharp decrease in revenue profile in 2018 to N104.157 Billion and later grow marginally to N109.845 Billion in 2019.

The components of the state revenue range from FAAC, VAT allocation, IGR, other FAAC transfer and grants. FAAC remain the major source of the state revenue. However, there was a sharp decrease in FAAC allocation between 2015 to 2016 due to worldwide economic recession and glut in Crude Oil price. Thankfully, this was cushion by improvement in IGR during theperiod.

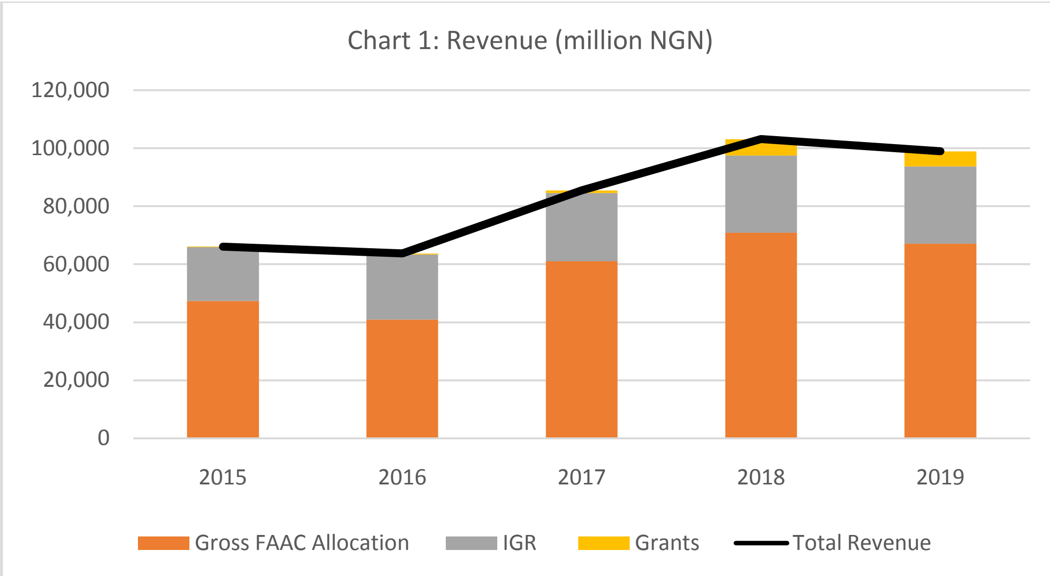
Internally Generated Revenue

The Internally Generated Revenue maintain a steady growth rate from Year 2015 – 2017 where it reached its Climax of N52.945 Billion. This was deteriorated by N47.74 in 2018. By Year 2019, there was an improvement in IGR which resulted into an increase from N27.43959 Billion in 2018 to N37.259 Billion.

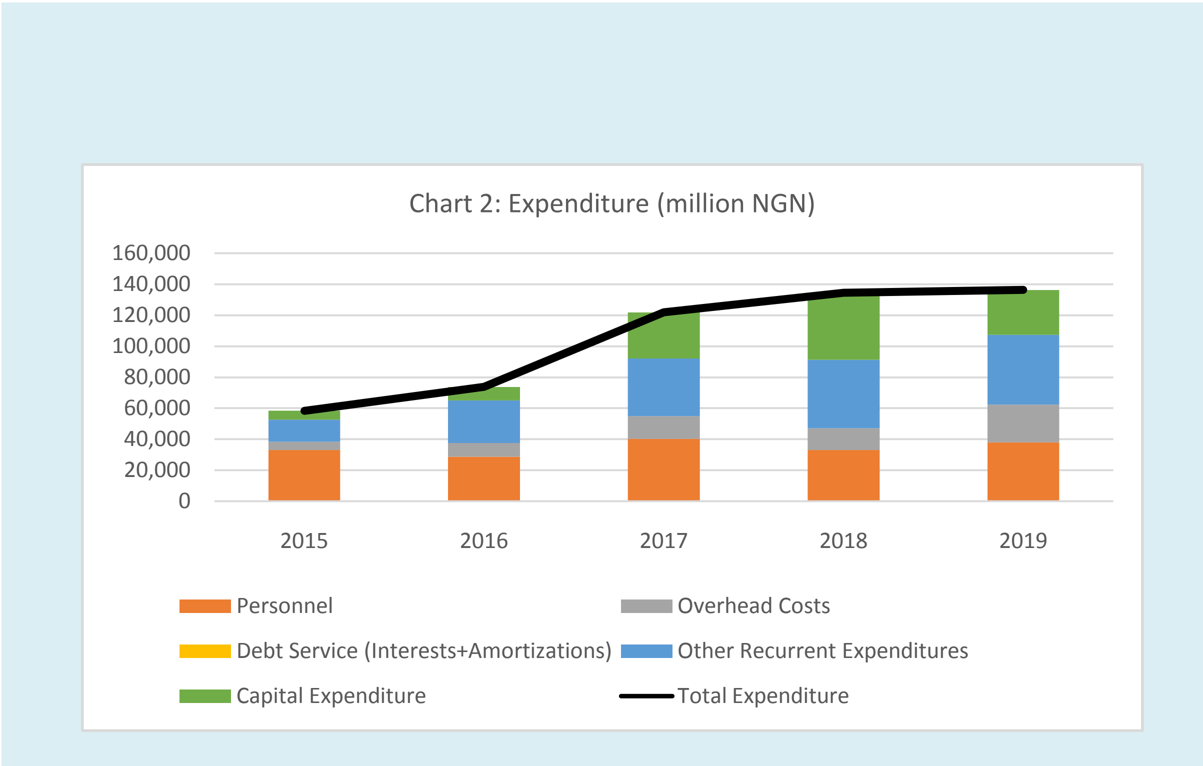
The enhanced in Revenue is largely due to restructuring in IGR collection process. This include the review of Commissions pay to Revenue Consultants, Organization of Informal Sector, adequate tracking of all tax payers through data bank etc.

3.1.2 Expenditure Performance

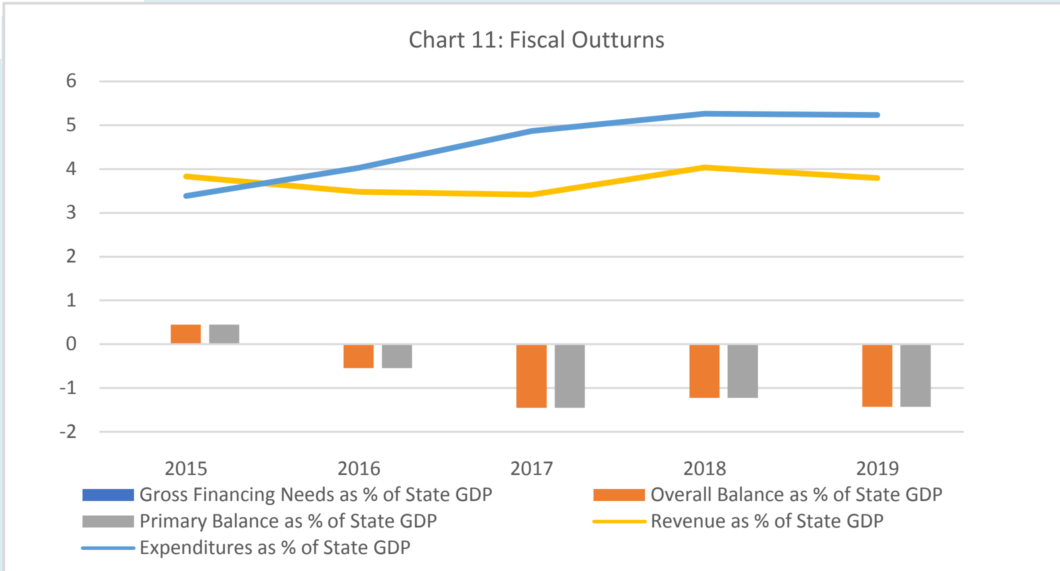
The state incurred the total expenditure of N538,195.46 Billion between Year 2015 – 2019. The expenditure trend increased steadily from Year 2015 to N26.188. This was a result of increment in the following items of the expenditure viz Personnel Cost, Other Recurrent Cost and Capital Expenditure. Due to continuous increase in the Capital expenditure and other recurrent expenditure, the expenditure profile of the state, continued to be sourcing from 2017 till 2019



The total revenue of the State in 2015 was N62.98 billion.There was a slight increase of 11.75% in the total revenue of the State in 2016. The revenue of the State rose to its peak in 2017 with the total revenue of N114.91B with a significant increase of N23.86B in the IGR which was 82.05% above the State performance in 2016. The total revenue slightly reduced by 9.36% in 2018 from N114.91B in 2017 but rose marginally in 2019 with 5.46%. However, it is significantly evidenced from the Chart that FAAC contributed the larger part of the revenue while the IGR was gaining an improvement for the period under review.



From the Chart above, the expenditure trend of the State between 2015 and 2019 was on upward trajectory. The total expenditure of the State was N59.29B in 2015 with about 55.78% expended on Personnel cost, 1.52% on Debt service, 9.75% on Capital expenditure while the remaining 32.95% was expendedon overhead and other recurrent expenditure. However, the State expenditure increased steadily from N59.29B in 2015 to its peak of N138.71B in 2018 but increase marginal from 2017 to 2019.



From the chart above, in 2015 revenue as a percentage of GDP was 4% while the expenditure as a percentage of GDP was 3%. Thereafter, the State experienced sharp growth in expenditure as a percentage of GDP from 3% to 5% while the revenue as a percentage of GDP declined from 4% to 3% in 2017. This trend was maintained till 2019 which indicates that the State expenditure is higher that the expenditure from 2017 to 2019.

i. Aggregate State Revenue: The analysis of the aggregated revenue of the State between 2015 and 2019 is as stated below:

REVENUE COMPOSITION	**AGGREGATED IN BILLION NAIRA**	**PERCENTAGE**
FAAC	287,365.24	68.85
IGR	117,712.80	28.21
GRANTS	12,258.88	2.94
TOTAL	**417,334.93**	**100**

The IGR of the state increased steadily as a result various reforms by the State Government such automation of revenue collection process, Treasury Single Account among others. However, the State receipt from the FAAC varies during the period due to the fall in global oil prices and economic recession.

ii. The State FAAC Allocations fluctuated in the last five years (2015 – 2019) due to the fact that federal receipts decline which is attributable to instability of crude oil price in the International Market. The State`s federal allocation including transfers from the excess crude account fell by 5.2 percent between 2018 – 2019.

iii. Internally Generated Revenue 2015 – 2019

The state IGR exhibited steady growth during the period under review. The IGR was N15.46 billion in 2015 and grew steadily to N37.49 billion in 2019 which shows a percentage increase of 142.8% between 2015 and 2019. The IGR trend as a share of aggregate revenue (excluding grant)increased steadily from 24.61% in 2015 to 34.8% in 2019. The improvement in IGR is mainly a result of tax and administration reforms aimed at improving collection rates and broadening the tax revenue base.

iv. Aggregate State Expenditure: The analysis of the aggregated expenditure of the State between 2015 and 2019 is presented in the table below:

EXPENDITURE	**AGGREGATED IN BILLION NAIRA**	**PERCENTAGE**
PERSONNEL	172,937.62	32.13
OVERHEAD	67,310.36	12.51
DEBT SERVICE	13,447,28	2.50
OTHER RECURRENT EXPENDITURE	168,014.03	31.22
CAPITAL EXPENDITURE	116,487.18	21.64
TOTAL	**538,195.46**	**100**

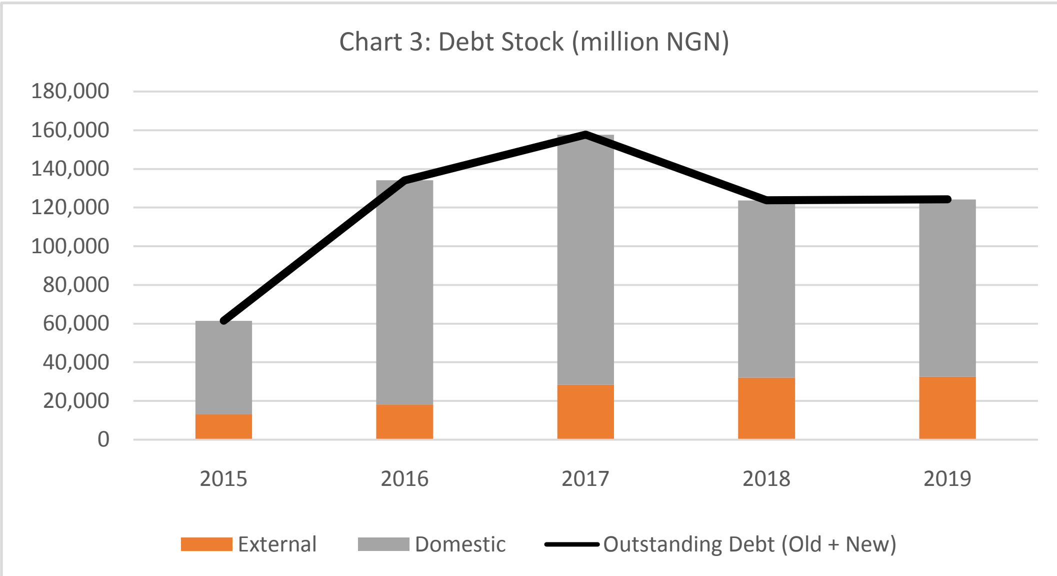
The State Expenditure increased steadily during the period under review. Between 2015 – 2019,real aggregate expenditure grew by 129.84%.

3.2. Existing Public Debt Portfolio

The evolution of the State public debt stock in terms of the total revenue and the GDP between 2015 and 2019 indicated and confirmed similar trends. For instance, the State Debt profile in terms of revenue was 98% in 2015 which rose to 190% in 2016 and declined steadily to 113% in 2019 while the State Debt stock in terms of GDP was 3.56% in Year 2015 which rose to a peak of 7.31% in 2016 and declined to 4.51% in Year 2019.

The debt portfolio of the State as at the end of Year 2019 is the sum of ₦124.2 Billion comprising of External Loan in the sum of ₦32.6 Billion which represent 26.3 percent of the total debt stock while the domestic debt stock is the sum of ₦91.6 Billion which is 73.7 percent of the debt portfolio of the State.

The public debt of the State includes the explicit financial commitments of the State like loans and securities that have paper contracts instrumenting the Government promises to repay. At the end of Year 2019 the principal payment is the sum of ₦19.8 Billion while the interest payment is the sum of ₦4.8Billion. The risk exposure of the existing debt stock of the State hinges on the State receipt from FAAC and changes in the exchange rate especially for the State external indebtedness.



The State total debt stock was on an upward trajectory between Year 2015 - 2017 where it attained its peak in Year 2017 in the sum of ₦157.1B and has steadily decline from 2018- 2019 by 78.77 percent. The decrease can be attributed to some fiscal reforms of the State Government which includes Adoption of Single Treasury Account and IPSAS cash basis and accrual methods Automation of Payroll System and revenue collection among others.

A cursory look at the Debt Sustainability Analysis of the State in the period under review indicated that the State Debt Service as a share of S-GDP, Revenue and Debt Service indicators were below the thresholds while the debt service as a share of revenue in Year 2016 – 2018 is above the threshold and the other two years i.e. 2015 and 2019 are below the threshold. It can be inferred that the total debt of the State is sustainable.

The State public debt as at the end of Year 2019 is the sum of N124.2 Billion and has been decreasing rapidly from it peak in Year 2017 in the sum of N157.7 Billion. The decrease in the debt stock particularly domestic debt from

Year 2017 to 2019 can be attributed to payment of salaries and other staff claim by the State Government, Payment of Contractors arrears and pension and gratuities by the State Government despite the sharp decline in the State receipt from FACC as a result of the failing oil prices. The increase in the external debt of the State is largely due to currency depreciation.

Arising from the above, the State Public debt portfolio largely consist of domestic loans consisting of Pensions and gratuity Arrears, Budget Support Facilities, and Salary bailout accounted for 69.18% of the State domestic indebtedness, while 92.07% of the State external loan is from loans from the World bank and International Development Association.

The State holds a low- cost, low- risk debt portfolio. The debt portfolio carried an average, implicit interest rate is 3.87 percent in Year 2018- 2019 and the interest repayments represented just 3.51 percent of the total expenditure. Exposure to currency fluctuations is limited because the foreign currency-denominated liabilities are only 26.29 percent of the total stock. Most internal loans and all external loans are fixed – rate obligations, thus not affected by changes in interest rate. As these loans have a maturity running from 10 to 40 -years and include financing from the Federal Government and multilateral organizations, rollover risk associated with potential deterioration of domestic financial conditions is negligible.

CHAPTER FOUR

4.0 Introduction – Concept of Debt Sustainability

Public debt by a State can be described as sustainable if the State Government is able to meet all its current and future payment obligations without exceptional financial assistance or going into default.

The key indicators used to evaluate a public debt sustainability are the present value of domestic and external debts, budget, revenue and debt service to external Debt. The primary purpose of the debt indicators and thresholds is to assess a State eligibility for the debt relief and to determine the amount of debt relief qualifying State are to receive.

With Indicative Thresholds	Without Thresholds
124,232/2,608,027 = 4.76%	24,569.64/67,173.08 = 36.58%
124,232/109,845 = 113.10%	4,785.74/109,845 = 4.36%
24,569.64/109,845 = 22.37%	2,695.58/109,845 = 2.45%
37,951.36/109,845 = 34.55%	

4.1 Medium Term Budget Forecast

In the medium-term horizon, the budget projections are hinged on the following general assumptions:

- Emphasis on achieving a more favourable balance for capital expenditure, through restraining the increasing trend in recurrent expenditure;
- Aligning State Government's income and expenditure by keeping spending limits within the dictates of available resources and within a fiscally sustainable debt position;
- Ensuring strict adherence to 'due-process' in budget execution as well as accountability, transparency and prudence in the entire public financial management process.
- Boosting IGR in accordance with the business case of Oyo State Board of Internal Revenue;

- Ensuring that the budget process is pursued within a framework that supports strategic prioritization and rational resources allocation and in accordance with the overall development policy objectives of the State.

4.1.1 Revenue Assumptions

a) **Statutory Allocation** – Premised on elasticity forecast using the crude oil benchmarks and macro-economic indicators in the Federal Macro-Economic Framework adopted by the State

b) **VAT** – Projection is hinged on elasticitybase forecast, using the national real GDP growth and inflation rates as the drivers for economic growth. With the increase of VAT from 5% to 7.5% and expansion of businesses, it is envisaged that there would be increased inflow of VAT

c) **Excess Crude** (including NNPC refunds, exchange rate differentials and other ad hoc distributions) – the estimate for 2021 is based on the collections from January to September 2020 and grossed up for the full year at the current rate.

d) **Internally Generated Revenue (IGR)** – In line with progress with the implementation of Treasury Single Account, IGR projections in the immediate term are expected to be slightly higher than the previous years through review of existing laws, plugging leakages and dealing with the phenomenon of tax avoidance and tax evasion as well as regulation and other initiatives. As usual, the IGR of the State accrued largely from PAYE, LGA statutory contributions, interest on deposits, etc. However, projection for medium-term will assume a higher IGR with the implementation of on-going property enumeration.

e) **Grants** – Consist of discretional and non-discretional. Most of the grants are non-discretional and are treated as contra-entries. However, adequate provision for Government Counterpart Cash Contribution to donor-funded programmes was embedded in the budget proposal in order to trigger the in-flow of expected revenue from this sub-sector. In addition, the rebasing and reclassification of some Capital Receipts should bring forward certain inflows into the 2021 fiscal year

f) **Financing (Net Loans)** – Like Grants, most of the loans are considered as non-discretional and are also not included in the Fiscal Framework, and as well not part of the envelope setting process.

4.1.2 Expenditure Assumptions

i. Consolidated Revenue Fund Charges - This includes public debt charges (which is external debt servicing) which is changing in the medium term and because increasing Internal Loan Components, this has led to increase in the amount budgeted for to increase slightly over the medium terms 2021-2023;

ii. Personnel – are largely based on the 2020 actual staff on the State Payroll with increase in critical areas particularly Education and Health Sectors and few other sectors including Security because of exigency of needs and succession plan.

iii. Overheads – Frantic efforts would be maintained to keep overhead cost in non-critical areas within reasonable limit**.** However, adequate fund would be provided for such programmes and activities that will create enabling environment for new economic activities that will empower the people for sustainable wealth creation and develop the capacity of all economic agents;

iv. Contingency and Planning Reserves –The target is 5% of recurrent revenue. The State desires to achieve much with capital spending. Recent trends indicate declining recourse to contingency funds.

v. Capital Expenditure – is based on the balance from the current account, plus the capital receipts. There is however the desire to achieve a more favourable balance for capital expenditure (at least above 50%)

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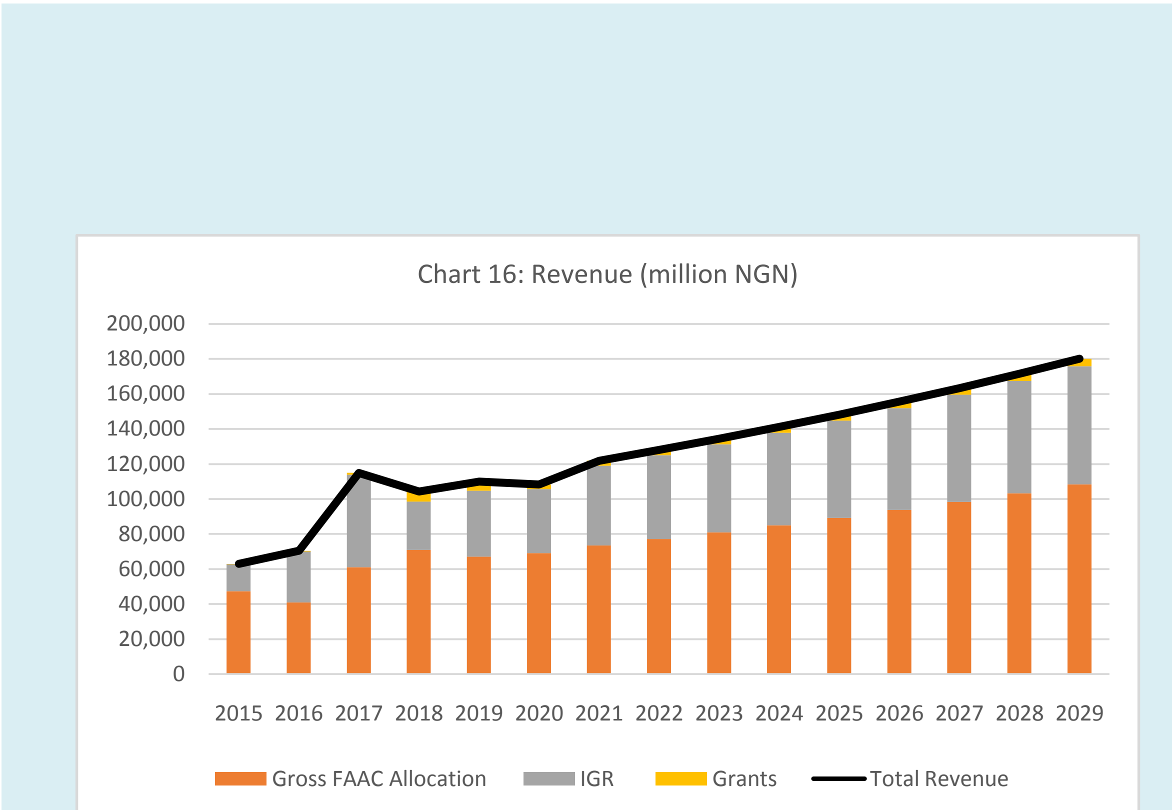

The revenue of the State is assumed to be on increase from 2020 to 2029 with percentage increase of 66.39 percent. The increase is hinges on the expectation that the FAAC and IGR will continue to increase.

OYO STATE TECHNICAL TEAM

1.	MINISTRY OF FINANCE	-	MR. OLAYIWOLA T. A.
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4.	MINISTRY OF BUDGET AND ECONOMIC PLANNING	-	MR. TIAMIYU W.A
5.	OFFICE OF THE ACCOUNTANT GENERAL	-	MRS SALAMI S.
6.	OFFICE OF THE ACCOUNTANT GENERAL	-	MR. ALLI S.A.
7.	STATE FOCAL PERSON (SIFTAS)	-	MR KILANKO O.O.