



DEPARTMENT OF THE TREASURY  
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OFFICE OF  
ASSISTANT SECRETARY  
FOR INTERNATIONAL AFFAIRS

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SUBJECT: SIG/IEP -- Working Group on Nigeria

At the April 14 meeting of the SIG/IEP, it was agreed that early consideration should be given to a strategy for addressing Nigeria's emerging financial crisis. For this purpose, you are invited to participate in a Working Group on Nigeria. The Working group will hold its first meeting on Wednesday, April 20, at 3:00 pm in Room 4426, Main Treasury.

In advance of this meeting, the State Department will circulate a strategy paper on Nigeria, and agencies will be asked to present their views on it. The immediate task of the Working Group will be to prepare a position paper or options paper that will be ready for SIG/IEP consideration during the week of May 2.

Agencies are requested to give the name of their representative(s) in advance of the April 20 meeting to Michael Monderer (566-5712).

*Donald C. Templeman*

Donald C. Templeman  
Acting Deputy Assistant Secretary  
Developing Nations

cc: Agriculture, Alan Tracy  
Federal Reserve, Donald Adams

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NIGERIA

The United States has a major stake in Nigeria's political and economic stability. Political moderation and stability in much of Africa would be jeopardized if Nigeria's democratic experiment collapses into disorder and radicalization. Nigeria's worsening economic problems have already spilled over to neighboring countries and an economic collapse would hit hard at these already depressed African economies. The additional pressure on the international financial system would also be an unwelcome development.

The key to avoiding instability in Nigeria is for the Nigerians to manage their affairs better. Our role should be to steadily nudge them in that direction. The situation, however, is complicated by Nigeria's August elections -- a serious test for Nigerian democracy -- and drastic and possibly haphazard cuts in import levels by at least one-third. Our Embassy estimates that food imports this year could be 20 percent below 1982 levels and 40 percent below 1981 figures. This is already producing shortages and raising prices in the marketplace.

Obviously, this is primarily a job for the IMF, but we are not confident President Shagari will or can make the major reforms the IMF would likely require until after elections. We also believe that Nigeria's pace of negotiations with the IMF must be brisk if Nigeria is to ensure against the emergence of financial gaps which can only be closed by too rapid and mismanaged import compression.

In this less-than-ideal situation for us and Nigeria, the following steps should be the core of our approach over the next six months:

1. We should immediately offer Nigeria a CCC credit (most of it on blended terms) in the range of \$200 million as a clear gesture of support for their effort to adhere to democracy and to be helpful with their immediate food problem. At the same time, we should avoid any negative actions on other transactions, including normal ExIm business, which would vitiate the political effect of our opening a delicate dialogue with Nigerian authorities on their need for economic reform and an IMF program. We would emphasize these latter points strongly when making the food credit available.

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2. Simultaneously, we would tell the Nigerians that we are willing to develop a larger financial package, but one which could only be made available as complementary financing for a Nigerian IMF Program. This could include a large follow-on CCC credit and a longer-term ExIm financing package. We can also offer to purchase Nigerian oil for the strategic petroleum reserve if the FGN is willing to sell at commercial prices. 7

3. Our people should also work quietly with the IMF and World Bank to encourage a thoroughgoing Nigerian program that gets to the heart of the problem of reducing waste by using the price mechanism instead of administrative fiat. Coupling an IMF program to a longer term World Bank plan for structural reform, including Nigeria's stifled agricultural sector, is called for.

4. We should also talk to the British to try to get them to seek an EC stance on Nigeria that parallels our own.

5. Our approach should also reinforce the stance of the private banks, who are also linking refinancing requests to Nigeria's assurances that it will turn to the IMF.

With regard to the initial CCC credit, the question of Nigeria's creditworthiness is properly raised. There is always some risk, although the Nigerians have kept reasonably current on all their bilateral official debts. When this CCC credit forms an important element of a strategy to get Nigeria back on solid and stable footing for the longer term, however, this question largely answers itself. Furthermore, if our strategy succeeds, it should bring handsome returns for United States agricultural trade as well as United States foreign policy.

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IMPACT OF DECLINING OIL PRICE ON  
NIGERIA

Executive Summary

Because of its weak marketing relationship with US and European buyers, Nigeria has experienced a particularly drastic decline in its oil revenues. Since oil provides 95% of exports and 70% of government revenues, this decline, combined with weak and wasteful economic management, threaten Nigeria's fragile democracy as it approaches August elections. Growing economic and social stress is evident including urban and rural violence, the burning of major government buildings (widely viewed as a way to cover evidence of corruption), rising unemployment and sudden ejection of hundreds of thousands of illegal immigrants. With neither Indonesia's conservative economic management and non-oil exports nor Venezuela's reliable export market for oil, Nigeria is in the most precarious position of these three petroleum producers.

A thoroughgoing economic reform, including a major devaluation and import liberalization, is needed to allow market forces to replace a hopelessly wasteful and corrupt system of resource allocation which is vitiating Nigeria's non-oil sectors, particularly agriculture, and threatens to sap the vitality of its democracy. Only the IMF -- with some follow-on help from the World Bank -- can help Nigeria work this out, but President Shagari is unlikely to accept an IMF program, and inevitable devaluation, before August elections.

The U.S. has a major stake in the survival of Nigeria's democratic system and the moderate, pro-western governments it has produced, despite that system's many imperfections. Our strategy, therefore, should proceed in two stages -- to help assure a peaceful election process now and to move Nigeria through suasion and conditional offers of help to negotiations with the IMF. An offer of a CCC blended credit now would help ease food shortages during the electoral period and give our Ambassador a vehicle to get the Nigerians to plan adequate food supplies. At the same time we will quietly urge the Nigerians to begin discussions with the IMF this spring, so that a program can be implemented -- at the latest -- promptly after elections. An additional package of U.S. measures should be conditioned upon Nigeria's conclusion of an IMF program.

Economic Situation: Oil Boom and Bust

The second oil boom almost tripled Nigeria's oil revenues, to \$24 billion in 1980 with average exports of 2 million barrels per day. GDP rose by 3.7% in 1980, and imports increased by 52%.

The economic situation deteriorated in 1981, as oil prices began declining while imports increased by 10%. The current account did a \$9 billion turn around, to a \$5 billion deficit and GDP declined by 2.4%. In April 1982, with foreign exchange reserves depleting rapidly, some austerity measures were taken,

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but they were clearly inadequate, as imports continued rising. The current account deficit reached \$7.4 billion, foreign exchange reserves fell below \$1 billion, and some \$3 to 5 billion in commercial arrears accumulated. (The Nigerians continue to pay amortization and interest on their \$8.5 billion long-term debt, both official and private, however).

The balance of payments outlook for 1983 is bleak. Nigerian oil exports in January and February fell to perhaps one-half of the 1982 level of 1.1 million barrels per day as other countries undercut prices. The Nigerian \$5.50 per barrel price reduction did not stimulate exports appreciably as buyers held off, waiting for further market price reductions.

Under these uncertain circumstances, we have projected, in Chart I, 1983 oil revenues based on three price scenarios (\$30, 25 and \$20 per barrel) on the assumption that Nigeria will be able to regain its traditional market share under the March 14 OPEC agreement. This would imply exports of about 1 million barrels per day. It remains to be seen whether the OPEC agreement will hold. If it does not, Nigeria could continue to have problems marketing its crude, and its oil revenue could fall even further than the \$20 pricing scenario.

Nigerian Balance of Payments Measures

In January, the Nigerian Government established a target of reducing 1983 imports by 30-40 percent, to an \$11 billion annual rate. With this assumption the 1983 current account deficit would range from \$2.4 billion to \$5.5 billion, with limited financing prospects. A \$2 billion Saudi loan has been much talked about, but is very uncertain. Given \$3 to \$5 billion in commercial arrears (which the Nigerians are attempting to convert into medium term debt) we doubt that new private sector financing will materialize in the absence of an IMF stabilization program.

Hence the government probably will have to further reduce imports. Although there is considerable scope for additional reductions in non-essential imports, we are skeptical that the Nigerians can rationally allocate foreign exchange to priority needs, given rampant graft and corruption in import licensing. Food imports, especially, may not have been adequately planned, and urban food scarcities could occur, heightening urban tensions in the pre-election period. Capital goods and raw materials imports have already been cut substantially, and in our worst case oil price scenario would have to be cut even further, effecting domestic production, employment and growth prospects.

What We Can Do

Prompt negotiation of a CCC blended food credit with 3-year repayment would help assure deliveries in the period before and

immediately after elections. We do not know exact food needs at this point, but it would probably have to be in the \$200 million range. It also would be our vehicle to get the Nigerians to plan adequate food supplies and improve their management of import cuts. A \$139 million credit was recently objected to by Treasury because of its concern that the Nigerians would be unable to repay. We could justify the risk, however, on the basis that a credit would also allow us to open a dialogue with the FGN about the need for an IMF program, as well as on the basis of our foreign policy interests in the success of moderate, pro-western democracy in Africa.

Even though Shagari will not be willing to devalue before August, the Nigerian Government should begin to plan with the IMF and the IBRD for prompt post-election measures. We discussed this with Shagari's principle political advisor, Shehu Musa, who visited the Department on March 16-17. This also can be raised in April when Foreign Minister Ishaya Aduv visits here. We also should urge the British to join the effort, given their strong interests in Nigeria and Africa.

There are several additional steps we should hold out contingent upon Nigerian acceptance of an IMF stabilization program:

- a. A follow-on CCC blended credit to help assure adequate food supplies after the elections. It would probably have to be at least equal to or greater than the First credit.
- b. A \$100 million Eximbank loan for essential spare parts, designed to help the Nigerian manufacturing sector survive the import crunch.
- c. Consideration of a 50,000 barrel per day government-to-government purchase of Nigerian crude oil for the Strategic Petroleum reserve (approximate value \$500 million). We would have to negotiate a price understanding with the Nigerians.
- d. We should encourage the IBRD to follow up the IMF program with a plan to help revive Nigeria's agriculture sector (which once accounted for 80% of Nigeria's exports). A small (\$20 million) PL 480 Title I program could be used to reinforce the IBRD's plan, and would give us some input into the effort, which could take the form of an international consultative group.

## CHART I

Nigeria's Balance of Payments  
(Billions of Dollars)

	1982	1983 (Alternative Scenarios)		
		\$30 Oil	\$25 Oil	\$20 Oil
Exports	14.0	12.1	10.5	9.0
Oil	13.5	11.6	10.0	8.5
Non-Oil	0.3	0.5	0.5	0.5
Imports	-16.1 *	-11.0	-11.0	-11.0
Trade Balance		+ 1.1	- 0.5	- 2.0
Services & Transfers of which interest	- 5.3	-3.5 (1.2)	-3.5 (1.2)	-3.5 (1.2)
Current Account	-7.4	-2.4	-4.0	-5.5
Principal Payments of which		-4.1	-4.1	-4.1
Long Term		(-1.1)	(-1.1)	(-1.1)
Short Term Arrears		(-3.0)	(-3.0)	(-3.0)
Outstanding Financing Requirement		-6.5	-8.1	-9.6
Probable Financing Sources:				
Debt Relief on S/T Arrears		+3.0	+3.0	+3.0
Direct Investment		0.5	0.5	0.5
Drawings on Project Related Commitments		+1.3	+1.3	+1.3
Remaining Financing Gap		-1.7	-3.3	-4.8
Possible Other Sources:				
IMF		.5	.5	.5
Saudi/OPEC AID		+2.0	+2.0	+2.0
Debt Relief/Arrears on L/T Principal and Interest		+2.3	+2.3	+2.3
Optimistic Financing Gap (Surplus)		(3.1)	(1.5)	0.5

\* Excludes \$3-5 billion in commercial arrears.

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CHART IIComposition of Nigerian Imports  
(\$millions)

	<u>1981</u>		<u>1982</u>		<u>1983(Planned)</u>	
Food	2,366	14%	1,350	9%	992	9%
Non-Food Consumables	4,142	24%	6,364	42%	4,524	39%
Raw Materials	4,602	27%	3,010	20%	2,315	20%
Capital Goods	5,866	35%	4,516	30%	3,654	32%
Total	16,973		15,240*		11,485	

\* NOTE: Does not include \$3-5 billion in accumulated commercial arrears.

Source: Lehman Brothers, Kuhn Loeb.

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CHART III

Nigeria: Economic Indicators

Average Annual Percent Change Except Where Noted

	1975-78	1979	1980	1981	1982e
Real GDP Growth	6.0	- 2.1	3.7	- 2.4	- 5.0 (?)
Inflation (Consumer Price Index)	21.0	11.1	11.4	20.8	25.0
Monetary Growth	38.0	23.4	43.9	11.5	13.5
External Public Debt (Disbursed) (billion U.S. \$)	1.0	2.2	3.7	5.0	12-14*
Oil Export Earnings (billion US \$)	--	17.0	24.0	17.0	13.5
International Reserves (\$ billions) a	4.2	5.5	10.2	3.9	1.0

(Excludes monetary gold)

Includes \$3-5 billion in commercial arrears.

Note: Nigerian statistics are very unreliable and there are significant discrepancies between various sources (IMF, BRL, CIA).

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U.S. Interests in Nigeria

-- Political/Strategic

Nigeria, representing a quarter of Africa's population, is one of the few functioning democracies on the continent. Its moderate and pragmatic government has been cooperative in promoting a wide range of US bilateral and regional objectives. Often cast in the role of a leader and spokesman for African moderates, Nigeria carries considerable weight on the continent. It aspires to a major non-aligned role and is an active and moderate voice in third-world fora.

Nigeria strongly supports peaceful resolution of disputes in Africa and elsewhere (Chad, the Western Sahara, Horn of Africa and Lebanon). It was the major troop contributor to the OAU peace-keeping force for Chad and shares our opposition to Libyan attempts at destabilization in Chad. It has recognized the Habre government, made small but timely financial contributions to it, and has encouraged others to do so in its effort to see a stable government of reconciliation in Chad as a barrier to further Libyan adventurism. Until recently Nigeria contributed to the peacekeeping and stabilization effort in Lebanon.

Nigeria is influential within the OAU and has been tireless in its efforts to see the organization continue as a voice of African, as distinct from radical interests. Its resistance to attempts by Libya to dominate the OAU at the Tripoli meetings resulted in charges from radicals that Nigeria was at fault for the failure of the Tripoli conferences. Nigerian's Foreign Minister has toured Africa seeking support for an OAU summit in Addis Ababa, away from Libyan influence. Nigeria's foreign policy goals include the elimination of remaining minority regimes in southern Africa. It has recently been dismayed by the slow progress of the negotiations over Namibia. Nevertheless, in the past it has pressed other African states to give the US negotiating effort an opportunity to succeed. It now faces considerable internal and external pressure to take a strong stand against what most Nigerians view as a disintegration of the negotiating process, and has been criticized for taking a "pro-western" stance. While Nigerian leadership may be skeptical regarding our tactics, we believe that Nigeria accepts that our efforts are in good faith. It recognizes the central role of the US in pursuing peaceful resolution of such disputes; it will continue to press for near term success.

In sum, Nigeria is an important actor influencing a wide variety of issues of importance to the United States. It is an incipient regional middle level power whose significance should be recognized.

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The success of Nigeria's constitutional democracy and its respect for human rights are important to the U.S. not only in themselves but also because of Nigeria's influence on the development of democratic institutions elsewhere in the developing world. Nigeria has adopted a constitution based on the U.S. model, modified to reflect its own needs. President Shagari, a strong advocate of democratic institutions, has actively supported President Reagan's initiative on Democracy by sending a special emissary to the Washington Conference on Free Elections to give a keynote speech. Democratic institutions in Nigeria are not firmly established, however, and the current period may represent but a window in the Nigerian experience which economic and political instability could close.

### -- Economic Interests

Oil dominates the U.S. Nigerian economic relationship. Nigeria is our second largest oil supplier, providing 12-15 percent of U.S. imports (18% in 1980). Geographically and politically it is a more secure oil source than the Middle East. The GON did not participate in the 1973/1974 Arab oil boycott. Given the possibility of future disruptions in Middle East oil supplies, this important consideration should not be ignored because of the current oil glut. Nigerian liftings could be increased to a 2 million bbl/day level in an emergency, and could make a critical difference in meeting our oil needs. The U.S. has in recent years purchased about fifty percent of Nigerian oil exports, resulting in U.S. trade deficits with Nigeria of \$7.7 billion in 1981 and \$5.7 billion in 1982.

Nigeria welcomes U.S. investment. American direct non-oil investment in Nigeria was estimated to have a market value of \$400-500 million (book value in excess of 218 million). Total assets of some 100 American affiliates, including foreign equity and loans, is about U.S. \$1.8 billion, nearly two thirds in the petroleum sector. U.S. bank exposure in Nigeria, was \$1,276.9 million as of June 1983, of which \$281.0 was to banks, \$830.7 was to public borrowers and \$165.2 to private non-bank borrowers.

Nigeria represents an important export market (\$1.3 billion in 1982). The government encourages increased trade with the United States and given our large trade deficit with Nigeria, we are seeking to increase our share of the Nigerian market. Our major exports to Nigeria in 1982 were wheat, rice, construction equipment, aircraft and corn in that order. (\$400 million total in agricultural products and \$900 million in aircraft and construction equipment.) Despite austerity measures, U.S. grains will continue to provide a sizeable portion of Nigeria's estimated \$1.0 billion food import market for 1983. The Nigeria-U.S. Business Council and a Joint Agricultural Consultative Committee support increased U.S. trade and investment in this potentially lucrative market.

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## Description of Country's Political and Economic Situation

### -- Political Situation

In August, for the first time in eighteen years, Nigeria will hold Federal and State elections completely under civilian auspices. Election tensions are heightened by economic austerity dictated by declining oil revenues, and by growing social unease. Several recent fires in government buildings, universally regarded as arson to destroy evidence of fraud, have intensified concern over rampant government corruption. Outbreaks of major violence such as last year's religious riots in the north, have raised concern for public security. Violent crime has dramatically increased. Recently, Nigeria expelled hundreds of thousands of illegal aliens who, it was claimed, were a threat to public security and a major cause of growing unemployment among Nigerians.

### State of the Government:

The Government of President Shagari has been struggling to maintain an image of stability and competence. Decisiveness is an important issue for the Shagari government because the mild-mannered, conciliatory style of Shagari himself has been interpreted as weakness. Nigerians remember vividly the downfall of the first civilian government in January 1966 and the ensuing years of coups, civil war, and military rule, which issued in large part from that government's inability to act. The imposition of import controls, despite their negative effects, has been viewed as an act of political courage. The expulsion of illegal aliens in January was viewed by Nigerians as a decisive step toward solving problems of public security and growing unemployment. Nonetheless, the government has appeared indecisive in other important areas. It has failed to halt the rash of arson or deal forthrightly with corruption. Mismanagement, corruption, and inefficiency are longstanding aspects of Nigerian life, ingrained in social, economic and political institutions. The economic downturn may suppress the most excessive expressions of corruption, but will not guarantee that prevailing attitudes will be attacked or changed in any basic way. Most importantly, the PCN is not coming to grips with the country's rapidly deteriorating economic situation.

### Elections:

Despite his problems, President Shagari remains the odds-on favorite in the August elections. He has proved himself effective at compromise, a national and not regional figure; and has avoided the cult of personality common to African politics. His strongest presidential rival, by contrast, is seen as too ethnically-based and single-minded. His governing party, though it has suffered some defections, is more unified and broadly-based than its five competitors. Most Nigerians view the two strongest challenging

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parties as ethnic stalking-horses. These two opposition parties and factions of the others have tried to form an election coalition, but so far have been unable to decide on a single Presidential candidate.

Nigeria's past is replete with political violence and the potential for campaign violence is ever-present. Tribal rivalries still dominate politics. Student violence is of concern to political leaders and public sector unions could cripple urban services if they become economically dissatisfied. The democratic system is still too young and fragile to assure election losers that their time in national power will come; they still will control some states. The high stakes of victory and the possible penalties of defeat may prompt potential losers to violence.

#### The Military:

The government controls the armed forces by keeping the senior officers satisfied, ensuring that the center of power in the military is in the hands of northern allies, that military units are ethnically mixed and by assuring a generous military share of the budget.

The armed forces consider themselves the final guarantor of Nigeria's stability, however and are watching the situation closely. Most Nigerians, including some of the young military view a return to military rule with mixed emotions, and do not want to regress. Political parties, the free press, and the private sector have a strong interest in avoiding military rule. Nevertheless, should the civilian government become hopelessly discredited or unable to maintain law and order, the army would move to prevent collapse of the Nigerian state. Whether it would act on behalf of the civilian authority or on its own would depend largely on the degree to which the situation had disintegrated.

In sum, Nigeria faces one of its most difficult periods since the independence in 1960. Competition among the multitude of interest groups (tribal, regional, religious, economic, political), intense at the best of times, is likely to increase as everyone scrambles for pieces of a smaller pie. The social fabric will be sorely tested. The fledgling political system, which has not been tested in free and fair elections, will be sorely strained. Continuing economic troubles will only exacerbate the already major problems, and could be the shock which brings down the whole house.

#### Economic Situation

Nigeria's oil boom peaked in 1980 with oil revenues of \$24 billion and year end foreign exchange reserves of \$8 billion. Since then the balance of payments and the domestic economy have deteriorated rapidly because of falling oil exports. Total

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exports fell to \$14 billion in 1982, while imports were reduced only marginally causing a \$7.4 billion current account deficit and virtually exhausting foreign exchange reserves while arrears of \$3 to \$5 billion accumulated. GDP declined by 5% in 1981 and probably fell a further 2% in 1982. The FGN has used its reserve tranche and other non-conditional balances from the IMF; foreign private credit has dried up.

Prospects for 1983 are bleak. We estimate that total exports in 1983 will be in the \$9 to \$12 billion range, depending on oil market events. In the absence of external financing, Nigeria will have to cut its imports by at least the 30-40% target announced by President Shagari in January 1983 and probably far below that. This will add to growing unemployment and possibly result in food shortages, if, as expected, the Government does not allocate foreign exchange rationally.

Thus Nigeria is faced with the need for prompt short run measures to deal with a severe import constraint and shortage of foreign exchange. In the longer run, the country needs to adjust to reduced oil revenues and restructure its economy towards less dependence on oil as the engine of growth.

### Oil Revenues

Projecting Nigeria's oil income during the present market situation is particularly difficult because the country is a marginal supplier in the eyes of many US and European buyers, and does not have the more stable marketing arrangements of Venezuela and Indonesia. Consequently, as Nigeria maintained the OPEC agreed price level while other producers shaded prices, its exports declined precipitously. Exports averaged 1.1 million B/D in 1982, but fell by one-half or possibly even more in January and February 1983. After Nigeria's February price cut of \$5.50 per barrel, production is believed to have increased to about 675,000 B/D, but the level of exports may still remain severely depressed as buyers wait for further oil market price declines. The volume of Nigeria's exports, therefore, will depend on its ability to match price competition of other producers, particularly in the North Sea.

In these uncertain circumstances, we posit below three oil pricing scenarios as the basis for predicting oil revenues in 1983, using OPEC marker crude as a base price. We note that all three of these scenarios presume the reemergence of an integrated and cohesive OPEC which allocates Nigeria a market share consistent with the OPEC production sharing accord. We cannot estimate the impact of full fledged price war. All these scenarios represent a dramatic improvement over the early 1983 performance. If the OPEC accord does not allow Nigeria to compensate for these early losses by overproducing during the rest of 1983, Nigeria's revenues could be 20 percent less than those considered below.

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-- \$30 per barrel. At this price, in expected market circumstances, we believe that oil exports would increase to about 1 million B/D. Oil revenues would fall from \$13.5 billion estimated for 1982 to about \$11.6 billion in 1983.

-- \$25 per barrel. At this price Nigeria's export level is projected to expand only very slightly, to 1.03 million B/D, and oil revenues decline by \$1.6 billion to \$10.0 billion.

-- \$20 per barrel. At this price Nigeria's exports increase to 1.07 million B/D. Oil revenues decline a further 1.5 billion to \$8.5 billion.

### Balance of Payments Implications

Chart I shows current account projections for the three alternative oil pricing scenarios. Total exports would range from \$9.0 to 12.1 billion. Imports are set at \$11 billion, the target fixed by President Shagari in January 1983. With services of \$3.5 billion, including interest on debt and foreign oil company payments, the current account deficit ranges from \$2.4 to \$5.5 billion.

Amortization on medium and long-term debt due this year is an estimated \$1.2 billion and short-term debt payable is about \$3 billion though this figure could in fact be considerably higher. These would raise Nigeria's total financial requirements in 1983 to between \$7 and \$10 billion.

In past years, Nigeria has financed its balance of payments deficits by contracting new debt, by drawing down reserves, and by building up enormous commercial and short-term arrears. Nigeria has largely exhausted these sources of finance. Commercial banks, troubled by Nigeria's economic mismanagement, are not disposed to extend it any additional credits, and reserves, at \$1 billion (less than one month's current imports) can not be drawn down further.

### Financing Prospects

#### A) Probable Sources of Financing

Rollover of Arrears: Outstanding debt owed or guaranteed by the Federal Government of Nigeria is believed to total about \$12 billion of which \$3-5 billion is thought to be short-term arrears. As of June 30, 1982 total claims by banks in the BIS area on Nigeria were \$6.7 billion of which the U.S. banks' share was \$1.3 billion and the UK banks share was \$1.5 billion. Disbursed USG credits total only \$15 million. Eximbank has an additional \$493 million in undisbursed credits.

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Under any likely scenario, Nigeria must either receive formal debt relief or continue to accumulate arrears on all short-term debt. The banks reportedly have offered Nigeria a restructuring of its short-term debt and arrears but the FGN has been holding out for a broader package including some new money. Some accommodation is likely as to the FGN and the banks have an interest in reaching an agreement.

New Bank Credits: In the absence of a major adjustment effort by the FGN in conjunction with the IMF, the banks are not likely to provide Nigeria with new credits. However, Nigeria will probably be able to draw approximately \$1.3 billion on existing project related commitments during 1983.

These likely sources of financing are not sufficient to allow imports at the \$11 billion level since a financing gap of between \$2.2 billion and \$5.3 billion remains. In the absence of additional financing, therefore, the FGN will be faced with having to match imports to foreign exchange revenue and would have to cut imports to between \$6 and \$9 billion to eliminate its current account deficit, assuming it continued to accumulate arrears on all debt service payments. Imports are now reportedly running at annual rates as low as \$6-7 billion. This could result in an import compression of about 60% in a single year, roughly equal to the magnitude that Mexico is now undergoing after receiving large net resource transfers from the IMF, official bilateral sources and the commercial banks.

#### B. Other Financing Prospects

Access to IMF Drawings: Nigeria has already drawn all Funds available to it not subject to a test of cooperation or rigorous conditionality (reserve tranche; oil facility contributions). It has not yet approached the IMF to put together a reform program to be supported by additional drawings. Nigeria is generally expected to vigorously resist accepting the IMF "medicine" prior to the August election. At some point after government inaction in the face of rapidly mounting shortages could present a greater political risk than the acceptance of Fund conditionality, particularly if Fund resources are leveraged by additional private and official flows. The timing of Nigeria's approach to the Fund would depend, among the things, on the level of import compression compared to what Nigeria believes it could manage on its own.

The IMF would definitely insist on a devaluation of the heavily over-valued Naira as a first and essential step towards dealing with both immediate and long-term restructuring problems. Devaluation would be the most efficient and equitable means of restricting imports, and is essential to reviving the domestic economy, particularly the agricultural sector, which has stagnated in recent years because of the availability of cheap food imports

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and the non-competitiveness of agricultural exports (80% of Nigerian exports in 1960) because of the overvalued exchange rate.

The FGN will resist devaluation before the August election, however, for several reasons: (a) its inflationary effects, particularly on the price of food in urban areas, (b) the present system of import and foreign exchange controls is the single most important source of graft and partonage still available to the FGN, (c) it would cause a loss of face for the Shegari regime. For these reasons it would approach the fund only if its only alternative were a loss of power.

As a member of OPEC Nigeria probably would not qualify for drawings under the Compensatory Financing Facility (CFF) designed to compensate for temporary export shortfalls, since revenues would have been sharply lower than they were in the past had the government not exercised considerable control over the market. The USG has taken a strong position within the IMF against such liberal use of the CFF. Moreover, it is not clear whether the Fund staff could construct an oil revenue recovery scenario to justify a CFF drawing on purely technical grounds.

Nigeria would, however, be eligible to draw up to \$891 million from the IMF over a 12 month period covered by an economic stabilization program. Even if Nigeria were to approach the IMF in earnest now it is difficult to envision a first drawing before June so that at most Nigeria could expect to draw \$500 million from the IMF this year.

Saudi Support

All three oil price scenarios presume the continued integrity of OPEC. These are indications that the Saudis might be prepared to provide a \$2 billion loan to Nigeria in the context of an OPEC price and production agreement. However, given the reduction in Saudi income resulting from current and expected price and production, prospects for such a loan are very uncertain.

Rescheduling/Arrears on Long-Term Debt: If all else fails, and imports fall to below the absolute minimum needed to keep the economy functioning, the FGN would be left with no choice but to seek a rescheduling of its medium to and long-term debt. It would be unlikely to obtain this in the absence of an IMF agreement. It could, of course, simply accumulate arrears on these debt service payments and risk permanent damage to its credit worthiness and access to capital markets, but its current record of keeping payments current on medium and long-term debt indicates that this would only be a desperation measure.

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Prospects for Import Compression

The composition of Nigerian imports in 1981 - 1983 is shown in Chart II. Consumer goods account for approximately 48 percent of the planned 1983 import bill (for Mexico the 1981 figure was only 13 percent), of which food imports, at \$900 million account for 9 percent. Non-food consumer goods could be reduced a great deal with minimal economic hardship. Nigeria's current unbalanced and corrupt system of import licensing is not likely to result in a rational allocation of foreign exchange to essential imports. As a result shortages of key food stuffs and capital goods and raw materials could occur.

In its latest budget presentation the government indicated that it was postponing 20 % of its capital budget pending the availability of foreign exchange. This would reduce Nigeria's planned imports by approximately \$1 billion below the \$11 billion target. Moreover, if Nigeria could reduce its non-food consumer goods imports to the 24% share of total imports that occurred in 1981, the 1983 import bill would be reduced by an additional \$2.3 billion below the FGN's \$11 billion target. These two sources of import reduction would compress imports to \$7.7 billion, a level sustainable under the \$30 and \$25 per barrel price scenarios given likely sources of financing. In the event that export revenues fall below the level posited in the \$25 per barrel scenario -- a distinct possibility -- Nigeria would be forced to compress imports by at least a further \$2 billion to the \$5.7 billion level last experienced in 1975 if none of the less likely financing possibilities materialize. The FGN would be far more likely to accumulate arrears on its long-term debt than run the risk of such a drastic import compression. This alone would allow imports at the \$7.7 billion level referred to above.

Developing a Strategy for Nigeria--Conclusions & Recommendations

The length and depth of Nigeria's economic crisis will depend on the level of future Nigerian oil revenues, the availability of new external finance and FGN willingness to take domestic stabilization measures, including a devaluation. Under any plausible range of assumptions, however, we should expect in the shortrun:

- A sharp, compression of imports, by perhaps 50%.
- Possible food shortages.
- Disruptions of Nigerian industries, due to shortages of imported goods.

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-- Increased unemployment.

-- Higher inflation as finished goods become scarce.

Complicating the crisis are two special considerations. First, the political pressures on the Shagari regime. With a critical election in August, the government will be very reluctant to invoke further austerity measures beforehand. Yet, by postponing austerity measures probably in conjunction with an IMF program, the compression of Nigeria's economy will be more severe. In the post-election period, Nigeria will have few remaining financing options if it has not already at least come close to an agreement with the Fund.

The government's questionable capacity to manage its economic crisis is the second major concern. If Nigeria properly manages and rations its resources the crisis may be containable. However, the capacity to carefully manage such a crisis may not exist. It would be difficult to overstate this government's lack of effective, timely economic decision-making, and inability to follow through with correct implementation. Nigeria's administrative weakness is compounded by rampant corruption. We cannot exclude such possibilities as a food crisis, literally while new Mercedes are being offloaded at the docks. Equally irrational behavior on the international side, such as permitting a default, also cannot be excluded. Perhaps more than any other single factor, Nigeria's questionable ability and will to manage its economic crisis will make the Nigerian case the most threatening one to broader U.S. economic interests. The loss of a moderate and stable Nigerian democracy would inflict enormous and diverse damage on our African policy and impact on our energy security strategy. It might also impose an unneeded strain on the Western financial system, particularly on the UK.

#### What We Can Do

We do not see any viable course of action open to us which will not ultimately include the IMF. Even in the unlikely event that the United States, Saudi Arabia and others agreed to bridge Nigeria's 1983 balance of payments gap, that bridge could lead to financial catastrophe in the future if not tied to badly needed domestic reform. Our global policies vis-a-vis the IMF and World Bank would also be undermined seriously by constructing for Nigeria an alternative to the IMF. Yet we are far from helpless and, in fact, dare not sit back passively and wait hopefully for Nigeria and the IMF to find each other and in time. We must construct a diplomatic and economic strategy which will simultaneously accelerate Nigerian/IMF accommodation and ameliorate the most politically sensitive shocks of a rapidly compressing Nigerian economy.

## The Elements

Diplomatic persuasion will be the main element of our strategy but we need resources both to push the Nigerians to the IMF, and to insure that food supplies are adequate in the pre and post election period. We could consider an immediate three-year CCC credit of about \$200 million under the new blended credit program for delivery prior to August. We would follow this up with a further CCC credit in conjunction with a post-election stabilization program, plus a small (\$20 million) FY 84 PL-480 Title I. (A PL 480 program would also greatly assist us in recapturing a very lucrative market for U.S. agriculture). This second phase of CCC/PL 480 credits would be linked to a Nigerian agreement to get an IMF program, as would all other assistance provided.

If a CCC credit subsequently had to be rescheduled, there could be congressional criticism. Nigeria may not need an official rescheduling, although there is some risk. One way to reduce the risk of rescheduling would be to seek a multilateral food credit package with the proviso, as in the Yugoslav package, that credit therein would not be rescheduled. This achieves our objective, however, only if it can be done promptly.

While we may not want to link a (pre-election) CCC credit rigidly to a Nigerian agreement to obtain an IMF program -- because of Nigerian election constraints -- we should seek some assurance (the firmer the better) that Nigeria will go to the Fund right after the election.

The second element would be a long term \$100 million loan from Eximbank for essential spare parts designed to help keep Nigerian factories open as import levels fall. This would be disbursed after the election and tied to Nigerian agreement and an IMF program.

The third element of our package is a Government-to-Government purchase of Nigerian crude for the Strategic Petroleum Reserve, at a modest rate of 50,000 barrels per day (bpd) for one year only and with no advance payment. Total annual value would be about \$500 million. We informed the Nigerians last summer of our willingness to purchase their oil for the SPR, but they were unwilling to meet our pricing requirements. They may be more willing now. Our agreement with Mexico was 50,000 bpd for five years with an advance payment of \$1 billion.

As a part of a second (post-election) phase of a multilateral package we will need to involve the Europeans in new export credits and guarantees on some agreed burden-sharing basis. We should also coordinate with the Saudis for some gesture on their part, particularly given their manifest interest in seeing a more economically stable Nigeria which would be less likely to precipitate oil price instability.

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Finally, we would, in conjunction with the UK, encourage the World Bank to investigate prospects for a new Structural Adjustment Loan for Nigeria and programs to strengthening Nigeria's agricultural sector, again in conjunction with an IMF program. A role for U.S. agribusiness might eventually be identified, perhaps with some catalytic role for AID and OPIC. Local currency generations from the PL-480 part of our food assistance program may also provide funding.

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