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Strengthening the Nigerian Sovereign Investment Authority: A Policy Analysis of the Nigerian
Excess Crude Account and the Nigerian Sovereign Investment Authority Act

A thesis submitted in partial satisfaction of the requirements for the degree Master of Arts in
African Studies

by

Cynthia C. Ugwuibe

2012

ABSTRACT OF THE THESIS

Strengthening The Nigerian Sovereign Investment Authority: A Policy Analysis Of The Nigerian
Excess Crude Account And The Nigerian Sovereign Investment Authority Act

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Cynthia C. Ugwuibe

Master of Arts in African Studies

University of California, Los Angeles 2012

Professor Michael L. Ross, Chair

This thesis is an analysis of Nigeria's governance of its natural resource funds (NRF). The first half will discuss the unique challenges faced by oil producing countries in managing their resource revenues and provide an overview of Nigeria's lackluster track record in this respect. Then, the role of sovereign wealth funds (SWF), in particular natural resource funds (NRF) in mitigating some of these challenges will be examined. The second half of this thesis focuses on Nigeria's management of its previous NRF, the Excess Crude Account, and analyzes the strength and weaknesses of the Nigerian Sovereign Investment Authority (NSIA) Act, the legislation that established the countries three new NRFs and the government entity to manage them. I conclude by offering pragmatic recommendations on how to improve the NSIA, which is under legal dispute.

This thesis of Cynthia C. Ugwuibe is approved.

Andrew Apter

Edmond Keller

Michael F. Lofchie

Michael L. Ross, Committee Chair

University of California, Los Angeles

2012

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Introduction

“All in all, I wish we had discovered water”

- Sheikh Zaki Yamani, former Oil Minister of Saudi Arabia

Yamani’s dismal statement points to the fact that oil and other forms of natural resources can be a double-edged sword for nations that export them. Oil dependency poses unique economic challenges¹ for heavy oil exporters: (1) oil is a volatile source of public revenue; (2) it can induce inflation, resulting in an unfavorable exchange rate regime and decreasing the competitiveness of the oil producing country’s traditional exporting sectors; (3) oil is an exhaustible capital asset which must be wisely invested before its depletion. If resource-rich countries appropriately manage and invest their resource revenues, such revenues can be a catalyst for economic growth and development; but if such countries squander their revenues or neglect to address the distinct economic and fiscal challenges associated with reliance on oil or minerals, their mineral assets will be perceived as a curse.

To better address these unique challenges of oil dependency, a growing number of resource-rich developing nations have established sovereign wealth funds (SWF), specifically natural resource funds (NRF), to help stabilize their budgets in the face of instability in the world oil market and to foster prudent current and future investments of oil windfalls. Since international oil prices fluctuate erratically, oil proceeds are a volatile source of government revenue. Many oil dependent nations such as Saudi Arabia and Venezuela have created stabilization funds, one type of NRF, to shore up excess oil revenues when oil prices skyrocket, and tap into those savings when prices plummet. Moreover, because minerals are nonrenewable

¹Other authors have discussed other distinct challenges associated with oil revenues and oil dependency. For example, see chapter 3 of the *Oil Curse: The Paradoxical Wealth of Nations* by Michael Ross for an analysis of the four properties of petroleum that make it a troublesome resource.

resources, mineral-rich countries have established future generation funds—SWFs which invest a proportion of their revenues in long-term interest-bearing assets so future citizens can enjoy the benefits even after their minerals are depleted.

For some oil producing countries, establishing a NRF with legislation is one of the first steps that they have taken to ensure appropriate oil revenue management once they discovered viable oil fields; however other countries have been oil-producers for decades, and only in recent years have created legally-backed NRFs. Nigeria falls into the latter category; the country has been oil dependent since the mid 1970s, but it was only in May 2011 that it passed legislation, the Nigerian Sovereign Investment Authority (NSIA) Act, to establish three new NRFs, and a government entity to manage them.

The proper implementation and management of the NSIA would be a welcomed development for both Nigerians and the world. Nigeria is one of the top oil exporters and in 2010 ranked as the 10th largest world producer of oil (U.S. Department of Energy and Information Administration, 2011). Yet despite its oil wealth or perhaps because of it, the country has been encumbered with rampant public corruption, protracted political instability in the oil-rich Niger Delta, weak democratic consolidation and widespread poverty. The majority of the population subsists in endemic poverty, with no electricity, poor roads and few basic services. The oil-rich Niger Delta is not only overflowing with natural resources but in poverty, misery and ecological degradation as well: the average Niger Deltan has a 25 percent chance of dying before age 40; the region has appalling literacy rates, severely limited access to healthcare, dilapidated educational facilities and rampant unemployment. (Watts 2008b, 10-15). Ironically, a UN study found that the local government areas with oil facilities have a greater propensity to have higher signs of poverty than those without it (Watts, 2008b, 15).

However, if the NSIA is well-managed, oil money may reach the Niger Delta and other regions of Nigeria in the form of better roads, constant electricity, and improved healthcare. In addition to financing domestic development, Nigeria's oil wealth may become a new, albeit small, source of foreign investment for public companies and financial institutions. In the last financial crisis, many banks relied on capital from SWFs. As SWFs become increasingly influential players in the global economy and if the current rise in oil prices persists, the manner in which Nigeria's NRFs are managed may have international ramifications.

Nevertheless, Nigeria's previous policies and attempts to adhere to prudent oil revenue management practices have been derailed by extralegal political deals, institutional instability, and poor implementation, all side-effects of the country's prevailing prebendal politics. The NSIA is likely to operate as a weak and ineffective institution if its' legal shortcomings—its' questionable constitutionality in light of the country's fiscal federalism and the vague provisions for proper revenue utilization in its founding legislation—are not adequately addressed. These issues (among others) need to be confronted to ensure that the NSIA will be institutionally safeguarded against politically-motivated mismanagement and that the country's dreams of development are not just mere delusions.

In the subsequent chapters, I hope to accomplish three things: (1) discuss NRFs as one mechanism to achieve prudent oil revenue management, (2) provide a policy analysis of Nigeria's governance of its NRFs, the Excess Crude Account (ECA) and the NSIA legislation, and (3) offer recommendations on how to strengthen the governance capacity of the country's newly created NRFs under the NSIA. Chapter one offers a detailed analysis of three major revenue management issues associated with oil dependence. However, as a petro-state's economic and fiscal outcomes are not divorced from its political and institutional context (Karl,

1997, 6), I present a brief characterization of Nigeria's political environment, an environment that has unfortunately bred corruption, economic inefficiency, and lackluster revenue management. Moving from a description of the political landscape, the chapter presents Nigeria's historical track record (1960-2003) in addressing the three economic challenges of revenue management. In chapter two, I discuss SWFs and NRFs in detail: first, I provide an overview of characteristics of SWFs as a group, followed by a discussion of the various types of SWFs with specific emphasis on NRFs and the rationale for establishing them. Chapter three takes a closer look at Nigeria's management of the ECA. In 2003, Nigeria established the Excess Crude Account (ECA) which had moderate success but was ultimately encumbered by political and legal entanglements. Also, this chapter includes an overview of the key provisions of the NSIA Act. Drawing from an understanding of Nigeria's political economy and in the light of best practices for SWFs, in chapter four, I assess the strengths and weaknesses of the NSIA Act and offer recommendations. This thesis concludes with pragmatic proposals to achieving some of the salient reforms outlined in chapter four. I hope that Nigerian civil society organizations, international civil society organizations, policymakers, and individuals interested in Nigerian politics in general find this policy analysis useful in their efforts to promote better oil revenue management in Nigeria.

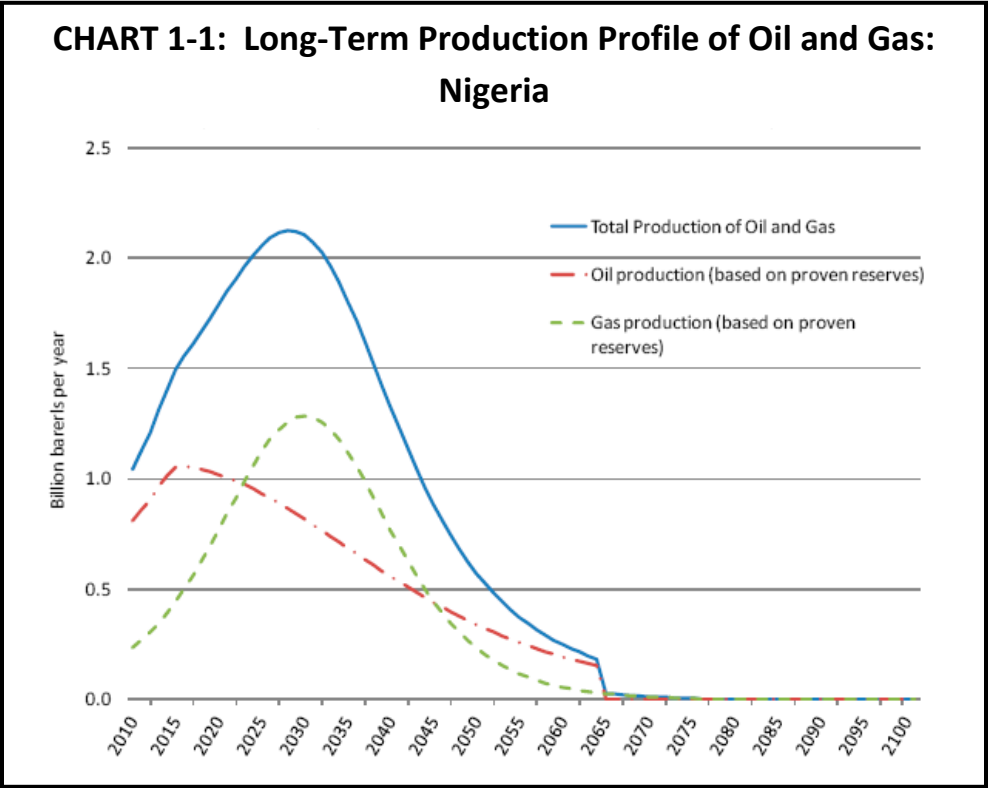
Chapter 1: The Distinct Fiscal and Macroeconomic Challenges of Oil Dependency and Nigeria's Oil Revenue Management History (1960-2003)

Countries that rely on oil receipts for a significant source of public revenue face unique economic challenges when compared with non-oil exporting nations (Karl, 1997; Davis, J. et al., 2003; Humphrey et al., 2007; Ross, 2012). These challenges are variability in oil extraction and streams of fiscal revenue; macroeconomic effects such as oil-revenue induced inflation, exchange rate appreciation and the Dutch Disease; and determining the optimal utilization of oil revenues given that oil is a non-renewable nature. These aspects of oil dependence require that oil producers implement a concerted and proactive revenue management strategy to optimally utilize their natural resources while mitigating the negative aspects of oil reliance. After discussing these three issues, I provide an overview of Nigeria's revenue management history since the first international oil boom of the 1970s which reveals that as Nigeria developed into an oil dependent state, it failed to properly tackle these challenges.

Three Challenging Aspects of Oil Reliance:

First, petroleum earnings are a volatile source of public revenue. This volatility originates from three sources: “the variation over time in rates of extraction, the variability in the timing of payments by corporations to [oil-producing governments], and fluctuations [on the international market] in the value of the natural resource produced” (Humphrey et al., 2007, 6). The rate of extraction throughout a nation's oil production period typically mirrors the volume of production, which itself fluctuates. In an oil producing country, production increases rapidly in the first few years eventually peaks, and then gradually declines until production ceases

(Humphrey et al, 2007). Chart 1-1 illustrates the long-term oil production profile for Nigeria as estimated by the International Monetary Fund (IMF); according to the IMF, Nigeria’s oil production should peak in the next few years, followed by a steady decline until projected depletion sometime between 2065 and 2075.



Source: 2010 IMF Article IV Consultation with Nigeria Staff Report

Also, the type of contract agreed upon between multinational oil corporations and the government can be a source of volatility (Johnston, 2007; Ross, 2012, 56-59). For instance, some contractual agreements exempt oil corporations from taxes for the first few years of production, thereby reducing the amount of oil revenue collected by government during that time frame (Humphreys et al, 2007). Additionally, the price of natural resource commodities especially oil fluctuates, making it difficult for resource abundant nations to estimate their fiscal budgets.

Compared with countries that export manufactured goods or other minerals, oil-producing states are at a disadvantage since the international price of oil is more volatile than that of manufactured goods (Lederman and William, 2007) and even more unpredictable than other volatile commodities (Gelb and Grasmann, 2010, 3; Ross, 2012, 6). Although the international prices of oil and gas have been upwardly mobile over time, world prices change often with as much as five to ten percent fluctuations in price on a weekly basis, and profoundly with soaring booms and devastating busts (Humphreys et al., 2007, 7). This price volatility makes it more difficult for commodity exporting countries to accurately project future financial streams. Also, this volatility reinforces pro-cyclical public expenditure patterns where spending closely parallels world oil prices. Oil producing nations that exhibit such patterns overspend during years of oil boom and are either forced to borrow during periods of falling world oil prices and oil revenues or otherwise abandon viable capital projects started in previous years and retrench important recurrent expenditures (Humphreys et al., 2007). Budina et al. (2006, 5-6) offer Nigeria as an illustration of pro-cyclical spending behavior.

Secondly, in addition to volatility, oil exporters are more susceptible to the Dutch Disease phenomenon. Dutch Disease is an economic occurrence coined after the experience in Norway when its manufacturing sector declined shortly after it began exporting natural gas in 1959 (Ezeala-Harrison, 1993, 199; Ross, 2012, 47-48). Although in Norway, the consequences of Dutch Disease were short-lived, the economic phenomenon has been applied to developing countries who after becoming natural resource exporters witness a decline in their non-oil exporting sectors. Specifically, Dutch Disease occurs as international demand for a country's oil exports brings in a large inflow of foreign currency. This influx appreciates the country's local currency against the foreign currencies thereby rendering the goods produced by the traditional,

non-oil, exporting sectors globally uncompetitive. In industrialized nations, the traditional exporting sector is manufacturing but in developing countries, the agricultural sector is typically this sector. The rise in the real exchange rate makes imports cheap, increasing the competition between foreign products and domestically produced goods. Also, if the government chooses to spend oil revenues on domestic development projects such as rebuilding public infrastructure, this could put pressure on the country's capital and labor resources available to the traditional export sectors. As these industries lose their profitability and are "crowded out" because of exchange rate appreciation on the global market and inflow of cheap imports and competition on the domestic front, they scale down their production. If the traditional export sectors are not appropriately incentivized through government policies, their decline will make it difficult for resource-rich countries to diversify their economies, reinforcing resource dependency.

Thirdly, petroleum is a nonrenewable resource and thus countries that currently rely on petroleum for revenue should not regard it as recurrent income but as a depletable asset which must be invested to yield high financial and social returns. Heal (2007, 157-158) asserts that gross domestic product (GDP) and gross national income (GNI) are insufficient indicators of a resource-rich country's national wealth because oil receipts are incorrectly classified as income and thus overstate the nation's economic welfare. Moreover, the sale of oil and gas should be considered asset disposal unless the revenue from selling resources is invested (Heal, 2007, 165). The level of development in an oil-producing nation and its people should dictate the suitable manner for investing oil revenues. According to Sachs (2007, 174-178), developmentally poor, resource-rich nations can benefit from government investments in education, healthcare and infrastructure to enhance its citizens' human capital and provide the crucial public goods needed to facilitate economic growth. For a high income, oil-producing nations, oil revenues should be

invested into long-term, high-return foreign assets; the interest earned from these investments will become a steady stream of public income which can to be used to finance pension and insurance programs (Sachs, 2007, 189-190). Regardless of the oil-producing nation's level of development, prudentially investing the natural resource stock can potentially yield high dividends for its citizens (Barnett and Ossowski, 2002). Also, the exhaustibility of petroleum raises the question of how governments can consume, invest, and save oil revenues in such a manner that they maintain intergenerational equity (i.e. future generations of citizens can reap the benefits of the oil wealth equally with the current generation).

Nigerian Patronage Politics Shape Economic Outcomes:

As the most populous country in Sub-Saharan Africa and often confronted with formidable economic, ethnic and security challenges, the Federal Republic of Nigeria has been frequently labeled Africa's troubled giant. The trouble with Nigeria is the state's prebendal and neopatrimonial political system which was exacerbated by the nation's initial tripartite federal structure and since the 1970s its oil dependency (Falola and Heaton, 2008). The country's prebendal politics explain (but by no means excuse) its disappointing economic record and oil revenue management given the set of development possibilities afforded by its resource wealth.

The Nigerian democratic state is characterized in part by prebendalism, the "persistent struggle to control and exploit the *offices* of the state" (Joseph, 1987, 1). Once obtained, political power in a neopatrimonial state² like Nigeria is viewed as personal property rather than as an impersonal feature of the state (Medard, 1982, 181). In this perspective, the aim of securing

² Medard argues that neopatrimonialism is a better concept than political clientelism to characterize the behavior of political actors in underdeveloped states such as Nigeria. Neo-patrimonialism" can aptly describe the other politically distorted behaviors such as tribalism and corruption coexist with clientelism but are not synonymous with it (Medard, 1982, 181; 187-188).

public office is not national service but in order to acquire access to state resources for private gain (Medard, 1982; Joseph, 1987; Watts, n.d.; Mbaku, 2007); unfortunately, this is the dominate attitude among Nigeria's political elite (Joseph, 1987; Saro-Wiwa, 1991). In his discussion about the various characterizations of political corruption, Mbaku (2007, 15-16) asserts that public office is perceived as a profit-making enterprise. From this perspective, public officials are not only wooed by pressures from powerful special interest groups who seek to capture the state³ but solicit such groups as customers or bribes from less affluent citizens (Mbaku, 2007, 15-15; 25; 46-48). Yet the office holder might be compelled to steal beyond the level that he desires in order to pay down a political debt: once in power, a political godson might be obliged by "godfather," to offer unbridled access to state resources as payment for his godfather's electoral sponsorship⁴ (Biereenu-Nnabugwu, M. and Onu, G., 2008).

Since the country's independence in 1960, prebendal politics has worked through ethnic and regional cleavages exacerbated by Nigeria's faulty federalist structure. The Nigeria entered nationhood with a tripartite federalist arrangement: this federal structure was a British colonial, administrative legacy that facilitated "indigenous colonialism" (Saro-Wiwa, 1991, 43), the political and economic domination of the Nigeria's ethnic minorities by the three major ethnic groups—the Igbo, Yoruba and Hausa-Fulani (Suberu, 2001; Apter, 2005; Falola and Heaton, 2008). Nigeria's independence-era federalism, where cultural brokers from the major ethnic groups agreed to become one country with three semi-autonomous regions (basically one region

³Mbaku distinguishes situations of state captures (i.e. when special interests design or control the policymaking process to yield government policies that unfairly reallocate the nation's wealth to them) from administrative corruption (i.e. when special interests seeks to shape the implementation of an existing policy and not necessary to control the entire policymaking process) (see Mbaku, 2007, 25).

⁴ See Biereenu-Nnabugwu, M. and Onu, G. Dialectal of Patronage Politics and Representative Democracy: The Case of Anambra State in Nigeria In: Okafor, V. O. eds. (2008) *Nigeria's Stumbling Democracy and its Implications for Africa's Democratic Movement*. Westport: Praeger Security International, p.56-78. for an account of godfatherism (the patron politics that paralyze Nigeria's political institutions and subvert the democratic process) in Anambra state.

for each major ethnic group), (Keller, 2007, 7) is a prime example of Stepan's "holding together" (Stepan, 2001, 19); such a federalist arrangement served the political and economic interests of the nationalist leaders (Suberu, 2001). "Yet behind the façade of political independence during the 1960s lay vicious interregional competition over political office, public contracts and state resources" (Watts, n.d., 421) as regional leaders desired to secure those resources for a narrow ethno-regional agenda (Falola and Heaton, 2008). This interregional competition to dominate at the central government level and to undermine other regions degenerated into two coups and a bloody two and half year civil war (Apter, 2005, 262).

Emerging from the civil war, the Nigerian government continued the fragmentation of the federation in order to create more balanced, multi-ethnic states. Whether the creation of more states actually resulted in greater political representation for the ethnic minorities than in the original tripartite arrangement (Keller, 2007, 14-15) or simply multiplied the points of access to allocated state revenues for ethnic majorities (Apter, 2005, 265) is debatable. However, the 1969 Petroleum Decree which placed all mineral rights in the hands of the federal government and the subsequent oil spikes of the 1970s did intensify pre-existing ethnic demands for more states and more splintering: marginalized ethnic minorities clamored for their own states and their own slice of the rich "national cake" through the revenue allocation process (Watts, 2008b, 10; Lewis, 2007). Also, on the individual level, the opportunities for wealth accumulation through public office were even more attractive now that the state was overflowing with oil monies; oil only made the stakes of securing political office greater.

Those who had access to the Nigerian state, could benefit from the state's headlong thrust into national development, an endeavor that was extravagant, poorly planned and perfectly expedient for embezzlement and corruption (Watts, n.d.; Apter, 2005; Lewis, 2007; Falola and

Heaton, 2008). However as the “oil high” wore off in the 1980s, the economic signs of the state’s rent-seeking behavior, extravagant wastefulness, and administrative inefficiency were conspicuous (Saro-Wiwa, 1991, 12). Lewis (2007, 284-285) asserts that corruption in Nigeria had crippling economic consequences because it was unorganized, unchecked and diffused; the state’s flagrant, “unsupervised” corruption resulted in gross administrative inefficiency (Medard, 1982; Joseph 1987).⁵ Under the military and civilian regimes in power during the oil booms, public accountability and supervision was significantly lacking such that public officeholders individually “served” as “access point” for private actors to gain acquire coveted state contracts and import licenses, while grossly neglecting their administrative duties (Lewis, 2007, p.284-285). This parasitic behavior engendered by the oil windfalls in Nigeria that “corrupted” the Nigerian bureaucracy (Saro-Wiwa, 1991).

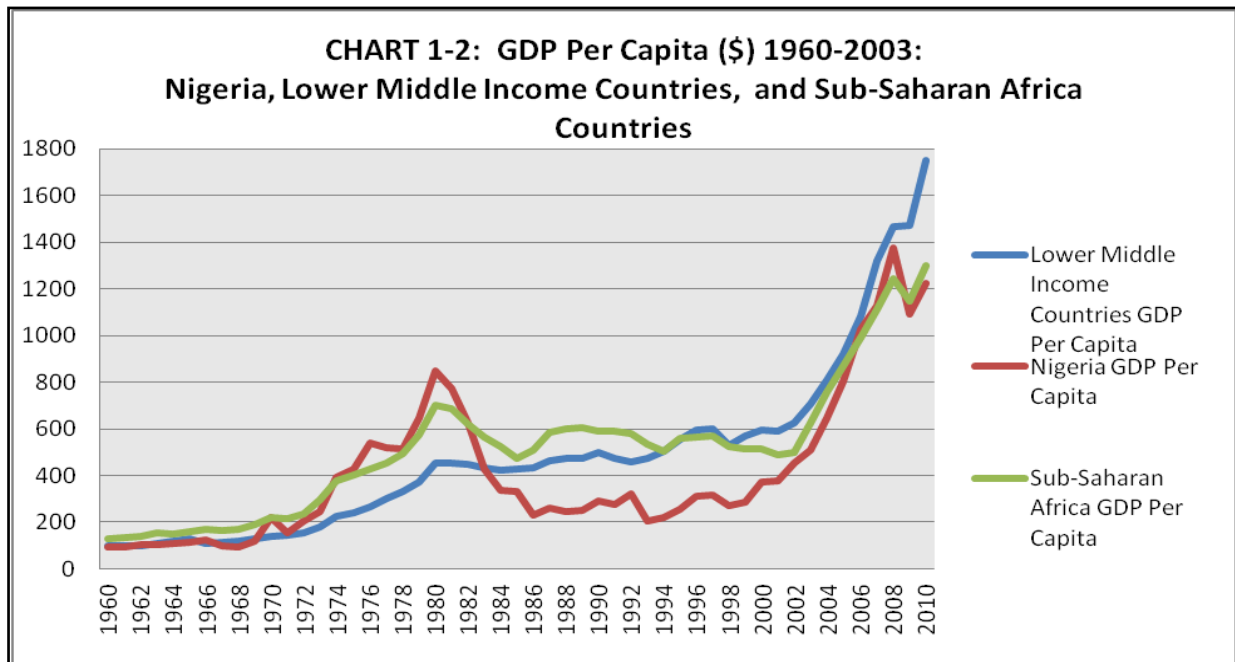
In addition to bureaucratic inefficiency, Nigeria’s prebendal politics has produced a captured state where approximately “85 percent of oil revenues accru[es] to 1 percent of the population,” (Watts, 2008b, 12) and distressing poverty is ensured for the majority, even the residents of the oil-producing Niger Delta. Despite the 1999 designation of 13 percent of the oil income to the Niger Delta states on the principle of derivation, very little of that accumulation trickles down to its inhabitants in a meaningful way (Watts, 2008a, 13). Local indignation at their plight—which Watt (2008a, 14) terms the “geo-political contradiction of oil without wealth”—has engendered in the Niger Delta ethno-nationalistic claims to greater oil rights or complete self-determination, reparations from multinational corporations (Saro-Wiwa, 1991; Apter, 2005, 261), youth mobilization and in more recent years militant insurgency (Watts,

⁵ In contrast to Nigeria, in Indonesia, a country that has striking similarities to Nigeria, bureaucratic corruption was streamlined and the illicit activities of public officers were loosely monitored and curtailed from severely disrupting economic efficiency (Lewis, 2007, 284-285).

2008a; Watts, 2008b). The extent to which the current insurgency in the region by groups such as the Movement for the Emancipation of the Niger Delta (MEND) is a result of legitimate grievances, organized crime and opportunism, a pure consequence of resource dependency, or a combustible blend of the three is a scholarly debate (see Watts, 2004; Collier, 2006; Ross, 2012) beyond the scope of this work. What can be said is that Nigeria's prebendal politics has only been intensified by oil dependency and fiscal federalism resulting in the country's overall plight: and rampant public corruption, political instability in the oil-rich Niger Delta, weak democratic consolidation and widespread poverty.

Given the country's politics, it's not surprising that Nigeria's economic development since independence has been intermittent, and lackluster; its 2010 GDP per capita of \$1,180 places it within the World Bank classification of a lower middle income country⁶ (World Bank Indicators, 2012). Compared to other Sub-Saharan African countries, Nigeria has performed slightly better in terms of GDP per capita since 2003. However, compared with lower middle income countries as a group, Nigeria's per capita GDP from 1960 to 2010 is slightly below the group average for most of the time period.

⁶ The World Bank classifies lower-middle income countries as those whose 2009 GNI per capita is between \$996 - \$3,945.



Source: World Bank Development Indicators and Global Finance Indicators

Nigeria’s History of Oil Revenue Management: 1970-2003:

Regrettably, Nigeria’s poor oil revenue management outcomes is a consequence of its unfavorable political environment. Since the oil booms of the 1970s and its entrance into the Organization of the Petroleum Exporting Countries (OPEC), Nigeria has intermittently struggled to implement prudent fiscal and macroeconomic policies which proactively address Dutch Disease, mitigate pro-cyclical budgetary patterns, and facilitate the productive investment and judicious saving of oil revenues.

Oil was discovered in 1956 in Nigeria, but agricultural exports—cocoa, palm oil, groundnuts and cotton—remained the primary source of government revenue until the international oil boom of the 1970s. In 1966 Nigeria was producing 415,000 barrels per day (bpd), 560,000 bpd by 1970, and two million bpd by 1972 (Falola and Heaton, 2008). As a member of the Organization of Petroleum Exporting Companies (OPEC), Nigeria benefited from

the 1973 OPEC embargo on Western countries and the subsequent spike in oil prices. Prices quadrupled from \$3.80 per barrel in October 1973 to \$14.73 in January 1974 and remained relatively high throughout the 1970s (Falola and Heaton, 2008). Again, in 1979, commodity prices doubled.

Yet the oil booms were mismanaged and led to the appreciation of the naira and the eventual decline in the agricultural sector. The oil booms of 1973-74 and 1979-81 brought in hefty royalty payments to the Nigerian government, leading oil to account for 82 percent of government revenue in 1974 (Falola and Heaton, 2008). With the surplus revenues, the government expanded the civil service and increased the salaries of civil servants; this increase in recurrent expenditures marked a transition to pro-cyclical spending pattern, a bad “fiscal habit” that Nigeria has since struggled to break. Additionally, Nigeria which was under military control increased capital investments in public work and infrastructural projects, construction, services, primary education and other capital-intensive industries; however some of these projects were only wasteful or too ambitious. Yet, with all its spending, the Nigerian government neglected the agriculture sector: it invested only three percent of public expenditures in agriculture in the 1970s (Pinto, 1987). This stream of public expenditure into urban industry increased the demand and price for domestic labor and contributed to a gradual but significant shift of labor away from agricultural production to these urban sectors that provided the prospects for higher incomes.

Moreover, the influx of foreign currency into Nigeria caused the real exchange rate to gradually appreciate. The official Nigerian naira to U.S. dollar exchange rate (adjusted for inflation) decreased approximately 61 percent from 1973 to 1984 (Pinto, 1987). The increased purchasing power of the naira had a twofold effect. First, the stronger naira made foreign goods

cheaper to purchase compared with before the oil price spikes and “unleashed a spasm of consumption and construction” (Watts, n.d., 419): Nigerians, particularly those with access to government contracts, import licenses and plum state jobs became avid consumers of imported goods: everything from lavish consumer goods to raw material for construction to foodstuffs was imported (Saro-Wiwa, 1991; Watts, n.d.; Apter, 2005). Second, it decreased the profit margins of Nigerian agricultural exporters: export crop producers now received fewer nairas in exchange for their dollar earnings. Incentivized by higher earnings in industry and construction, export farmers migrated to urban areas to fill demands for labor in urban construction. By 1980, agricultural production had dwindled to 20 percent of GDP, a significant decline from its 1960 high of 63 percent of GDP (Ezeala-Harrison, 2006). From 1970 to 1982, yearly production of cocoa, cotton, groundnut declined by 43, 65, and 64 percent respectively (Pinto, 1987). The collapse of the export agricultural sector was not a surprise and only signaled that Nigeria was in fact suffering from Dutch Disease. However, the retrenchment of agriculture could have been mitigated if the federal government had strategically devalued the naira to absorb some of the appreciation caused by oil prices as well as subsidized the export agricultural sector.

Nigeria’s decade of resource mismanagement became strikingly obvious after the oil bust of 1981 and the decline of the agriculture sector. As a result of the collapse in international petroleum prices, daily oil production output dropped from over two million bpd to 1.3 million bpd and GDP contracted by 8.5 percent from 1981 to 1983 (Pinto, 1987). Between contract fraud by government officials and the financial burdens of expanding the civil service and increasing salaries, the windfall profits from the oil booms were completely squandered by the end of Nigeria’s second twirl with a democratic government (1979-1983). Rather than implement austerity measures and scale back on ambitious development projects, both state and

federal governments turned to international borrowing, using future oil earnings as collateral (The Economist Intelligence Unit, 2002). External debt doubled from 9 billion to 18 billion, and from 1984 to 1993 public debt reached a staggering 140 percent of GDP (Falola and Heaton, 2008). The average Nigerian felt the economic downturn in terms of rising unemployment and inflation as the state and private companies was unable to pay civil servants and their employees, respectively (Falola and Heaton, 2008).

In the latter half of the 1980s, the Nigerian government, led by successive military dictators, Major General Buhari and General Ibrahim Badamasi Babangida, finally turned to austere macroeconomic and fiscal policies to reverse the economic downturn and decades of financial mismanagement. After an ostentatious program of public debates over structural adjustment, in 1986, the country pursued its own home-grown structural adjustment program (SAP) which included the devaluation of the naira, removal of marketing boards which disincentivized agricultural production, and privatization of state-owned enterprises (Watts, n.d.; Economist Intelligence Unit, 1996; Falola and Heaton, 2008). Yet structural adjustment did little to restructure the Nigerian state into a professionalized bureaucracy: Apter (2005, 247) asserts that Babangida's reforms to the civil service, only streamlined the process of misappropriation of state funds as ministers served as both the head and accounting unit of their ministries and they no longer had to pad the pockets of the Accounting Office. Thus, the system of state corruption was perhaps reorganized but not reformed, regrettably ensuring that the economic reforms made would not have lasting, positive consequences for the nation's development.

As the political turmoil and pressures for democratic rule in the early 1990s overshadowed the reform process, economic reforms became increasingly less effective. Although, Babangida promised elections, in a ploy to extend his time in power, he rewrote the

rules and officiated the democratic game—away from the [civilian-led], participatory model that [he initially] avowed and toward the carefully staged con of a political “419”⁷ [on the Nigerian people] in which elections were more simulated than real” (Apter, 2005, 238). After mandating a two-party system in the 1989 Constitution, disqualifying all associations that petitioned to qualify as one of the two legal party, consecutive election annulments and postponements, Babangida’s orchestrated the greatest political 419, the annulment of the June 12th 1993 election, often cited as the most credible election in Nigeria’s history (Apter 2005, 237-245).

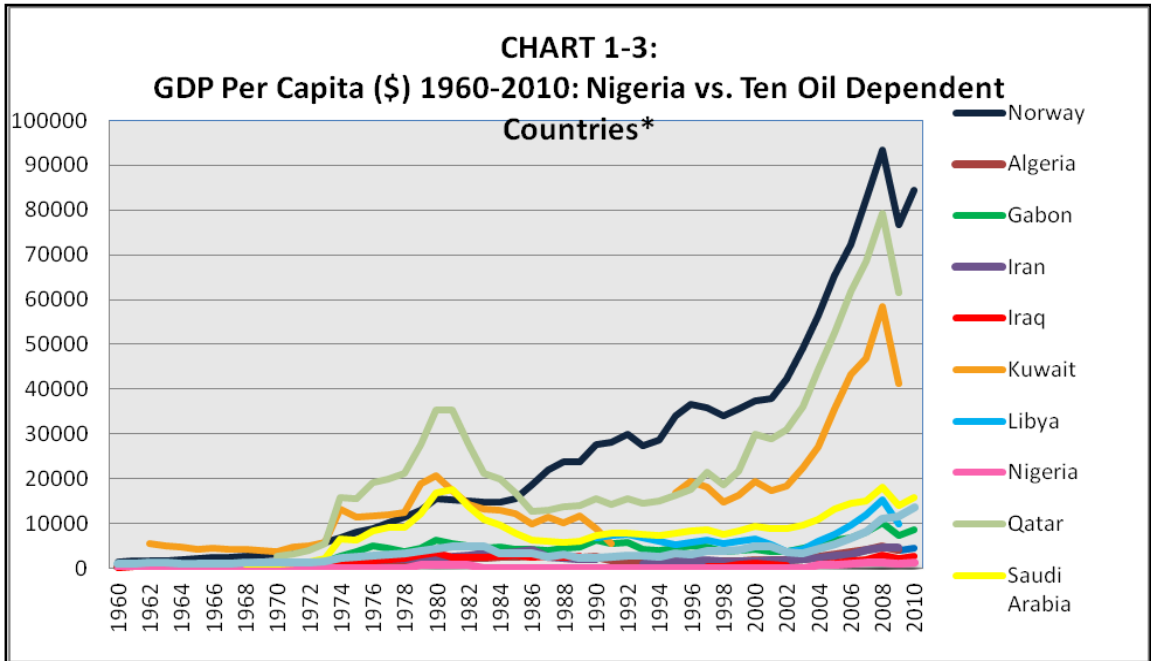
The unscrupulous management of the electoral process during this time is equally matched by the country’s unprincipled fiscal revenue management. In 1989, Nigeria created a stabilization fund with the aim to save realized oil revenues above the \$16 per barrel oil benchmark price (World Bank, 2003). Unfortunately, the fund rules did not incentivize fiscal discipline as there were no penalties for premature withdrawals from the fund (World Bank, 2003). In the fund’s initial year, the government averaged \$21.50 per barrel of oil and accumulated 14.6 billion naira in savings; yet in the same year, the federal government withdrew 6 billion naira from the fund (World Bank, 2003). Also, in subsequent years the stabilization fund was not appropriately managed; disregarding the reference price rule in order to withdraw from the fund during periods of rising oil revenue rendered the fund an ineffective tool in altering Nigeria’s pro-cyclical public spending pattern.

In late 1993, when General Sani Abacha seized power, the Nigerian government regressed further into fiscal indiscipline as it ran budget deficits, re-appreciated the currency and delayed any further privatization of public enterprises, reversing the limited economic reforms achieved in the late 1980s (Economist Intelligence Unit, 1996; Economist Intelligence Unit,

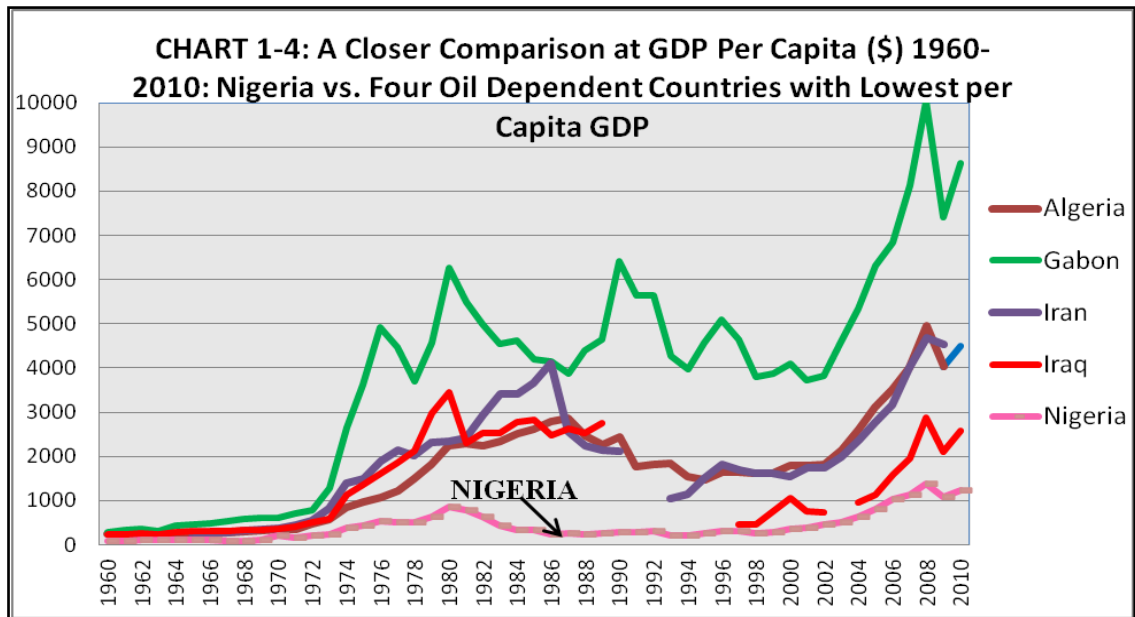
⁷ 419 is refers to the section of the Nigerian criminal code which criminalizing fraud. It is the colloquially name for advance fee-fraud made infamous by Nigerian

1999). Also, despite the transition to democratic rule in 1999, the Obasanjo administration in his first term (1999-2003) failed to improve oil revenue management and achieve its market-oriented economic agenda because its policy strategies were not integrated into a sound public budgeting process nor supported by a commitment to fiscal discipline (Economist Intelligence Unit, 2002). During his second administration (2003-2007), Obasanjo implemented key tools to promote improved fiscal oil revenue management with initial success; however, his successes have been hampered or reversed by political opposition from the state governors and constitutional issues (more on this will be discussed in subsequent chapters). For the majority of its oil-producing lifespan, Nigeria has not committed to the sustained fiscal discipline needed to prudently manage its oil revenues for productive uses for its citizens.

The case of Nigeria illustrates that oil dependency and revenue management can be cumbersome, however the challenges associated with oil revenue are not insurmountable as countries such as Indonesia and Norway have manifested the political will and implemented the necessary tools to ensure that their resource wealth is a blessing rather than a curse (Ross, 2012). If utilizing the income per capita to assess how effectively oil-rich governments has invested its natural resources for the benefit of its citizens since 1970s, Nigeria lags behind. Although, Nigeria's GDP per capita trajectory is fairly typical for a lower middle income country and for a Sub-Saharan African country, it consistently has the lowest income per capita among top oil dependent countries (see Chart 1-3 and Chart 1-4).



Source: World Bank Development Indicators and Global Finance Indicators



Source: World Bank Development Indicators and Global Finance Indicators; gaps represents years with missing data.

The ten countries compared to Nigeria in Chart 1-3, were chosen because they, like Nigeria, have consistently maintained a moderate to high degree of oil dependency since 1970, a few years before the first oil booms of that decade. In particular, for each of these countries from 1970 to 2010, petroleum products comprised approximately 50 percent or greater of their exports. Despite that all these countries have remained moderately to heavily oil dependent, at least three of them have either effectively invested their oil revenues or diversified their economies in such a manner that has improved per capita GDP values. For instance, Norway's impressive 2010 GDP per capita is approximately \$76,800 which is over 23 times the value of its 1970 income per capita figure of \$3200 (World Bank, 2012). In contrast, Nigeria's 2010 per capita GDP was only roughly 5 times greater than its 1970 values of \$218 (World Bank, 2012). Although, all the nations had a noticeable increase in GDP per capita from 2000-2008 which reflects the boom in international oil prices of that time period, Norway, Qatar and Kuwait had the most dramatic increases in income per capita. In short, among top oil dependent nations, Nigeria's poverty (in part due to poor oil revenue management) is an atypical case.

In the last decade, perhaps as a consequence of the most recent oil price boom, more resource-rich countries have established natural resource funds(NRFs), sovereign wealth funds (SWF) sourced from oil sales, to help them manage their growing oil revenues and to achieve their specific policy agendas. Although some countries, such as Norway have had NRFs for a few decades more, a sizeable number of oil producers are new fund managers. Chapter two provides an overview of SWFs before diving into a descriptive examination of NRFs.

Chapter 2: Nuts and Bolts of Sovereign Wealth Funds (SWFs) and Natural Resource Funds (NRFs)

In the first half of this chapter, I present the SWF definitions and classifications that will be used throughout this paper, the group characteristics of SWFs, and variations among SWFs in terms of fund objectives, investment strategy, institutional framework and governance structure. The second half of the chapter takes a closer look at NRFs which are SWFs created from commodity revenues. The chapter concludes with analysis of the political-economic rationale for establishing NRFs.

Group Characteristics of SWFs:

Andrew Rozanov is often credited with coining the term “sovereign wealth fund” in his 2005 article “Who Holds the Wealth of Nations?” (WLC, 2010; Rozanov, 2005). Rozanov is the head of Sovereign Advisory at State Street Global Markets, the investment research division of State Street Corporation, a leading financial services holding company. In his article, he described SWFs as funds created from either accumulated national budget surpluses, profits from natural resource extraction, or in a few cases donor aid (Rozanov, 2005, 1). SWFs are formed to either “insulate the budget and economy from excess volatility in revenues, help monetary authorities sterilize unwanted liquidity, build up savings for future generations, or [set aside]...money for economic and social development” (Rozanov, 2005,1).

According to the Sovereign Wealth Fund Institute, a organization that conducts research on SWFs and provides related consultancy services, sovereign wealth funds (SWF) are “state-owned investment fund[s] composed of financial assets such as stocks, bonds, real estate, or other financial instruments funded by foreign exchange assets (Sovereign Wealth Fund Institute,

2008).”⁸ This definition emphasizes the variation in asset composition of SWFs rather than the national objectives underlining their creation. Clay Lowery, former Assistant Secretary for International Affairs at the U.S. Treasury Department, would add to the SWF Institute’s definition that SWF assets are usually managed separately from official reserves (i.e. they are not foreign reserves used for traditional monetary purposes)⁹ (U.S. Department of Treasury, 2008). SWF managers have also defined themselves: according to the International Working Group for Sovereign Wealth Funds (IWG), a voluntary group of SWFs, SWFs are:

“[S]pecial purpose investment funds or arrangements, owned by the general government. Created by the general government for macroeconomic purposes, SWFs hold, manage, or administer assets to achieve financial objectives, and employ a set of investment strategies which include investing in foreign financial assets. The SWFs are commonly established out of balance of payments surpluses, official foreign currency operations, the proceeds of privatizations, fiscal surpluses, and/or receipts resulting from commodity exports” (IWG, 2008).

The IMF offers a similar definition but also classifies SWFs into five categories based on their policy objectives: stabilization funds, savings funds for future generations, development funds, reserve investment corporations and contingent pension reserve funds. Stabilization funds are funds that set aside resources for stabilizing the budget; savings funds, often called “rainy day funds,” are established to ensure intergenerational equity of resource revenues; development funds are created to finance large-scale development projects or to facilitate industrial growth;

⁸ Since 2005 the literature on SWFs has proliferated, however there is still no standard definition for what constitutes an SWF. The lack of consensus in the literature is partly because SWFs are a heterogeneous group of public investors which vary in their institutional and governance structure, asset size, asset allocation, investment strategy, and policy objectives. Christopher Balding in “A Portfolio Analysis of Sovereign Wealth Funds,” mentions that some definitions are very restrictive, excluding domestic assets such as state-owned enterprises or pension funds while other definitions are too broad and classify any type of government-owned or controlled assets as SWFs (Balding, 2008).

⁹ Some SWFs do function as a last resort stabilizer of official reserves.

reserve investment corporations aim to increase financial returns on the country’s reserves; and pension reserve funds are created to invest a portion of current public revenues to meet the government’s future pension liabilities (IMF, 2008b). For this paper, I rely on a combination of the IMF, IWG and SWF Institute definitions for SWFs.¹⁰ I rely on the IMF’s policy objectives classification to categorize the SWFs (see Tables 2-1 and 2-2 below) and the IWG definition when examining the variety of SWFs’ legal and institutional framework.

Source of Funds	AUM in \$ billions	Country	Fund Name	Date of Inception	Type of Fund (according to IMF SWF classification)
Oil	\$627	UAE – Abu Dhabi	Abu Dhabi Investment Authority	1976	Savings
Oil	\$560	Norway	Norway Government Pension Fund-Global	1990	Stabilization, Savings and Pension Reserve
Oil	\$472.5	Saudi Arabia	SAMA Foreign Holdings	n/a	Stabilization*
Oil	\$296	Kuwait	Kuwait Investment Authority (2 separate funds: Reserve for Future Generations and the General Reserve Fund)	1953	Stabilization and Savings
Oil & Gas	\$88.3	Russia	National Welfare Fund	2008	Pension Reserve
Oil	\$85	Qatar	Qatar Investment Authority	2005	Savings
Oil	\$70	UAE – Dubai	Investment Corporation of Dubai	2006	Reserve Investment

¹⁰ Although the SWF Institute’s definition does not mention a classification for SWFs, its SWF rankings by asset size listed on its’ website appears to be consistent with the IMF SWF classification mentioned this paper.

Oil	\$65	Libya	Libyan Investment Authority	2006	Savings
Oil & Gas	\$61.4	Russia	Reserve Fund	2008	Stabilization
Oil	\$58	UAE – Abu Dhabi	International Petroleum Investment Company	1984	Reserve Investment
Oil	\$56.7	Algeria	Fund for the Regulation of Receipts	2000	Stabilization
Oil	\$38.6	Kazakhstan	Kazakhstan National Fund	2000	Stabilization
Oil	\$30.2	Azerbaijan	State Oil Fund	1999	Stabilization and Savings
Oil	\$30	Brunei	Brunei General Reserve Fund	1983	Unknown
Oil	\$23	Iran	Oil Stabilization Fund	1999	Stabilization
Copper	\$21.8	Chile	Social and Economic Stabilization Fund; And Pension Reserve Fund	1985 (re-created in 2006)	Stabilization; Pension Reserve
Oil	\$15.1	Canada	Alberta Heritage Fund	1976	Pension Reserve
Oil & Gas	\$8.2	Oman	State General Reserve Fund	1980	Savings
Diamonds & Other Minerals	\$6.9	Botswana	Pula Fund	1994	Savings and Stabilization
Oil & Gas	\$6.3	East Timor	Timor-Leste Petroleum Fund	2005	Savings and Stabilization
Oil	\$6.0	Mexico	Oil Revenues Stabilization Fund of Mexico	2000	Stabilization
Oil	\$5.3	Saudi Arabia	Public Investment Fund	1971	National Development
Oil	\$2.9	Trinidad & Tobago	Heritage and Stabilization Fund	2000 (re-created in 2007)	Stabilization and Savings
Oil	\$1.2	UAE – Ras Al Khaimah	RAK Investment Authority	2005	Unknown
Oil	\$1	Nigeria	Nigerian Sovereign Investment Authority (3 separate funds)	2011 (legally enacted; will be operational)	Savings; Stabilization; Development;

				05/2012)	
Oil	\$0.8	Venezuela	FEM- Macroeconomic Stabilization Fund	1998	Stabilization
Phosphates	\$0.4	Kiribati	Revenue Equalization Reserve Fund	1956	Savings
Oil	\$0.4	Gabon	Gabon Sovereign Wealth Fund	1998	Savings
Oil & Gas	\$0.3	Mauritania	National Fund for Hydrocarbon Reserves	2006	Stabilization and Savings
Oil	\$0.08	Equatorial Guinea	Fund for Future Generations	2002	Savings
Oil	unknown	UAE – Federal	Emirates Investment Authority	2007	Reserve Investment*
Oil	unknown	Oman	Oman Investment Fund	2006	n/a
Oil	unknown	UAE – Abu Dhabi	Abu Dhabi Investment Council	2007	Reserve Investment*
Gas	unknown	Papua New Guinea	Papua New Guinea Sovereign Wealth Fund (2 separate funds: Stabilization Fund; a Development Fund)	2011	Stabilization; Development
Mining	unknown	Mongolia	Fiscal Stability Fund	2011	Stabilization
Oil	unknown	Ghana	Ghana Heritage Fund	2011	Savings
Oil	unknown	Ghana	Ghana Stabilization Fund	2011	Stabilization
Non- commodity	\$567.9*	China	SAFE Investment Company	1997	Reserve Investment
Non- commodity	\$459.6	China	China Investment Corporation	2007	Reserve Investment
Non- commodity	\$293.3	China – Hong Kong	Hong Kong Monetary Authority Investment Portfolio	1993	Reserve Investment
Non- commodity	\$247.5	Singapore	Government of Singapore Investment Corporation	1981	Reserve Investment
Non- commodity	\$157.2	Singapore	Temasek Holdings	1974	Development and Savings*
Non-	\$134.5	China	National Social	2000	Savings and

commodity			Security Fund		Pension Reserve*
Budget surplus	\$73	Australia	Australian Future Fund	2006	Pension Reserve
Excess foreign exchange reserves	\$43	South Korea	Korea Investment Corporation	2005	Reserve Investment
Non-commodity	\$36.8	Malaysia	Khazanah Nasional BHD	1993	Savings and Reserve Investment*
Non-commodity	\$30	Ireland	National Pension Reserve Fund	2001	Pension Reserve
Non-commodity	\$28	France	Strategic Investment Fund	2008	N/A
Non-commodity	\$13.5	New Zealand	New Zealand Superannuation Fund	2003	Pension Reserve
Excess foreign currency reserves	\$11.3	Brazil	Sovereign Fund of Brazil	2008	N/A
Non-commodity	\$9.1	Bahrain	Mumtalakat Holding Company	2006	Savings
Non-commodity	\$7.61	Australia	Building Australia Fund	2008	Development
Non-commodity	\$4.69	Australia	Education Investment Fund	2008	Development
Non-commodity	\$4.01	Australia	Health and Hospitals Fund	2008	Development
Non-commodity	\$1.4	Italy	Italian Strategic Fund	2011	N/A
Non-commodity	\$0.5	Vietnam	State Capital Investment Corporation	2006	Development
Non-Commodity	\$0.3	Indonesia	Government Investment Unit	2006	Development

Source: Author's compilations from SWF Institute website, official websites of SWFs, and IMF documents. AUM values as of February 2012

*Best estimate or categorization by author based on information gathered from several sources

TABLE 2-2: State SWFs ranked by source of funds (commodity/non-commodity/mixed) and then by assets under management (AUM) size					
Source of Funds	AUM in \$ billions	State	Fund Name	Date of Inception	Type of Fund (according to IMF SWF classification)
Oil	\$40.3	US – Alaska	Alaska Permanent Fund	1976	Savings
Minerals	\$4.7	US- Wyoming	Permanent Wyoming Mineral Trust Fund	1974	Stabilization and Savings
Oil & Gas	\$2.5	US – Alabama	Alabama Trust Fund	1985	Savings and Stabilization
Oil & Gas	\$0.1	US – North Dakota	North Dakota Legacy Fund	2011	Savings
Oil and other non-commodity sources	\$14.3	US – New Mexico	New Mexico State Investment Council (3 separate funds: The Severance Tax Permanent Fund; Tobacco Settlement Permanent Fund; Land Grant Permanent Fund)	1958	Savings*
Oil and other sources	\$5.27	US – Alaska	Constitutional Budget Reserve Fund	1991	Stabilization

Source: Author’s compilations from SWF Institute website, official websites of SWFs, and IMF documents; AUM values as of February 2012.

Although the term was coined fairly recently, SWFs that is—publically-owned investment funds with the national objectives Rozanov mentions or the institutional set-up that the IMF describes—have been in existence for several decades. Based on my SWF definition which adopts the IMF’s SWF classification, the oldest SWF is the Kuwait Investment Authority created in 1953 and not the California Public Employee Retirement System (CalPERS), the public pension fund of the state of California established in 1932. The IMF makes a clear distinction between public pension funds such as CalPERS and public pension reserve funds.

The former are not considered to be a SWF because with such funds the government (represented by either the executive branch or the central bank) is not the direct beneficiary.¹¹ Other authors have recognized CalPERS as the oldest SWF; Edwin Truman (2007) in his article, “A Scoreboard for Sovereign Wealth Funds,” includes CalPERS as an SWF.

Moreover, as a group, SWFs are financed from a variety of sources such as from the sale of fuel and non-fuel commodities (i.e. NRFs) or from the accumulation of non-commodity foreign currency reserves or budget surpluses. Based on my definition of SWFs, there are currently 63 SWFs in the world established by 6 U.S. states and 41 nations; out of the 63, 43 funds are NRFs and 20 are non-commodity funds (see Table 2-1 and Table 2-2). Although non-commodity funds are fewer in number, they are still quite sizeable in asset value. Out of the ten most valuable SWFs, six are derived from non-commodity sources. However, the most valuable SWF, the United Arab Emirates (UAE) Abu Dhabi Investment Authority, is an NRF created in 1976 and currently estimated at \$627 billion. \$627 billion amounts to approximately 210 percent of UAE’s 2010 GDP.¹² The second largest SWF, China’s SAFE Investment Company is well behind the Abu Dhabi Investment Authority with an estimated total value of \$567.9 billion. However, China which has a total of four SWFs (three of which are among the top ten most valuable SWFs) is truly wealthier than UAE: China’s four SWFs total to approximately \$1.4 trillion assets (SWF Institute, 2012).¹³ To put this in context, China’s 2010 GDP was approximately \$5.9 trillion, second only to the U.S. whose 2010 GDP was \$14.86 trillion (World

¹¹ According to Ashby Monk, CalPERS is not owned or controlled by the state of California nor is it the sole direct beneficiary of the fund (Monk, 2008). In depositing in the fund, the government of California roughly matches the contributions by public employees who are CalPERS members; these CalPERS members are the direct beneficiaries (Monk, 2008). The IMF regards pension reserve funds as SWFs since the government is the direct beneficiary of the investments made to finance future pension liabilities and the citizens (via the government’s provision of pension payments) are the indirect beneficiaries (Monk, 2008).

¹² Statistic calculated by author using World Bank Data from <http://data.worldbank.org/country/ united-arab-emirates>

¹³ In addition to the Abu Dhabi Investment Authority, UAE has six more SWFs of which four have a total value of \$156.3 billion. Two of the six funds have undisclosed assets amounts (SWF Institute)

Bank, 2012). Yet, the majority of SWFs (both commodity-based and non-commodity funds) have assets below \$100 billion. Ranking the SWFs based on their AUM size, the Nigerian Sovereign Investment Authority (NSIA) which will be operational with \$1 billion seed money is the 48th largest SWF. Additionally, as of February 2012, SWFs as a group have approximately \$4.828 trillion AUM and this number has risen steadily since 2000. Compared with other institutional investors, SWFs are larger than both hedge funds and private equity firms, but smaller than mutual funds, pension funds, and insurance funds (The CityUK, 2012).

SWFs can be categorized based on their inception into two periods: funds formed before 2000, and those created after. The majority of the SWFs (23 out of 43 NRFs and 15 out the 20 non-commodity funds) were created in the post-2000 period spurred by the rapid increase in oil prices in the early 2000s to 2008 and the rise of market economies particularly in Asia (CityUK, 2012; Wharton Leadership Center[WLC], 2010; Santiso, 2008). In fact, nine SWFs were either legally enacted or institutionally set-up in 2011 alone. Interestingly, Santiso characterizes SWFs as primarily emerging market institutions¹⁴ since the majority of SWFs are not established by developed countries or OECD countries (Santiso, 2008).

Variation in Investment Strategy, Institutional Framework, and Governance Structure among

SWFs:

As previously mentioned, non-resource rich countries establish SWFs to achieve different purposes and meet different financial needs of the sovereign nation. However, even if resource

¹⁴ Emerging markets was a term first coined by World Bank economist, Antoine van Agtmael, in 1981 as a reference to countries such as Thailand with \$10,000 in per capita income (Wharton Business School, 2008). Nowadays this term broadly alludes to countries (such as Mexico and Chile) that are strengthening their political and economic institutions and shows great development potential (Wharton School, 2008). Thus emerging market economies are creating SWFs more than advanced countries.

rich countries create development funds or reserve investment corporations, they will typically establish two types of SWFs as well: funds that are purposed to be “trust fund” for future generations or to help diversify the economy away from resource dependency (savings funds) and funds which support fiscal budget stabilization and to prevent surplus oil revenues from entering the domestic economy and inducing inflation (stabilization funds). Stabilization and savings funds are NRFs since they are typically financed by revenues from resource commodities.

SWFs invest in different types (classes) of assets such as public and private equities, public securities, real estate, infrastructure, hedge funds, cash, bank deposits (such as certificates of deposits) (CityUK, 2012). However, SWFs invest in public equities and public securities such as fixed income assets at a disproportionately higher rate than they do in other types of assets. Fixed income assets are assets where the issuer must pay regular interest payments to the purchaser. Some examples of fixed income assets include government bonds, debt securities that mature after 10 years, debt securities maturing between one and ten years, and government bills such as U.S. treasury bills which mature in less than one year. For bonds, the return of the principal paid is usually guaranteed at its maturity and for government bills, the purchaser buys the bill at a discounted value and then receives the full value at maturity. Fixed assets especially the public debt securities from stable, developed countries with little risk of the government default are considered one of the safest investment opportunities; but they also carry lower returns. To invest in equities is to purchase an ownership stake or stock in a company. When compared with equity investments, fixed income assets offer lower yields as well as reduced risk. These two asset classes are less risky investment options than other hedge fund and private equity assets. However, SWFs differ in their investment strategies based on the investment

philosophy of the fund and the national objectives of the fund which may determine the fund's risk profile, investment time horizon, and can place liquidity constraints on the fund's assets.

In addition to differences in investment strategies, among SWFs, the legal mandate and institutional framework varies considerably. Based on the results from a survey taken by the 21 members of the IWG in 2008, Hammer et al. (2008) write that all members establish their SWF with some form of domestic legal backing: members created their SWFs via constitutive laws, fiscal responsibility legislation, management agreements between finance ministry and the central bank, company law or in a few cases enshrining it in the constitution. The policy objectives for which the funds are established are outlined in the founding legislation. Approximately 50 percent of the respondents mentioned that their SWFs are institutionally separate from the central bank and the executive government while the other half expressed that their country's SWF are simply pools of assets and not institutionally independent (Hammer et al, 2008).

In terms of the governance structure, those funds that are institutionally independent from the state are more likely to be established as corporations or under a constitutive law with separate governance structure (Hammer et al, 2008). Yet, institutional set-up is not a proxy for governance structure: SWFs which are established as corporations can still be managed by the finance minister in conjunction with monetary authorities; a good example being the Government of Singapore Investment Corporation (SWF Institute, 2012). Funds which are structured as pool of assets are either under the complete managerial oversight of the ministry of finance and operational control of the central bank or maintain quasi-independent relationship with these two institutions (Hammer et al, 2008). For instance, Australia's pension reserve fund, the Future Fund, and its three development funds, are managed somewhat jointly by the national

treasurer, finance minister, and an independent board (Australia Future Fund website, 2012). The duties of the treasurer and finance minister are to appoint members of the board who must not be government officials and to develop the investment strategy for the fund; the board members are tasked with carrying out these investment mandates (Australia Future Fund website, 2012). According to survey respondents, many SWFs try to strike a balance between creating operational independence for the SWF with government accountability (Hammer et al, 2008). This is achieved through a variety of ways such as creating a separate legal entity, delegating the management responsibilities to the central bank or to an independent board on which a government official is a member, or mandating that financial audits be reported to either to the finance minister, the president or the legislature (Hammer et al, 2008). Beyond the distinctions mentioned above, Ross (2004) mentions that SWFs can differ in other ways: each country can determine if it wants the SWF to hold assets in-country or abroad and the level of discretion given to the SWFs in investing assets.

NRFs: Stabilization & Savings Funds:

As this paper will focus mainly on NRFs, the following is a more in-depth discussion of the two main types of NRFs, stabilization and savings fund. Some countries establish separate funds to fulfill a saving and stabilization objectives; for instance, Ghana, a new oil exporter, established in 2011 the Ghana Stabilization Fund as well as a separate savings fund, the Ghana Heritage Fund. Other countries set up one multi-purpose fund which serves both stabilization and savings objectives. Botswana's Pula Fund established from the government's diamond proceeds is a good example of a multi-purpose fund (Mohohlo, 2007).

Stabilization funds help to insulate the government from the volatility associated with depending on commodity earnings for public revenue (Barnett et al., 2001). Natural resources especially oil are a volatile source of public revenue because the prices for such commodities fluctuate on the international market and consequently the government revenue derived from their sale (Barnett et al., 2001; Humphreys et al., 2007). The volatility in commodity prices can impede commodity exporting countries from accurately projecting future financial streams. Also, if it is not adequately contained, this volatility reinforces pro-cyclical government spending behavior where the level of public spending closely parallels the fluctuations in world price for a country's commodity export. Resource-rich nations that exhibit pro-cyclical spending behavior overspend when the international commodity prices skyrocket and are either forced to borrow when prices collapse or otherwise abandon viable capital projects started in previous years and retrench important recurrent expenditures (Humphreys et al., 2007).

However, if a stabilization fund is established, in commodity boom periods, prudent governments transfer the surplus revenue into the stabilization fund rather than boost spending to match the increased oil receipts. By doing so, governments mitigate the inflationary pressures associated with introducing too much monies into the domestic economy. In periods when world prices fall below the projected threshold, the stabilization fund can finance the budget shortfall, thus allowing expenditures to be independent from international commodity prices. Due to short-term liquidity concerns, these types of funds are more likely to invest in low-risk/low-yield assets than other types of funds. Additionally, Dixon and Monk (2011, 6) assert that a stabilization fund can serve as a "lender of last resort" for a resource-dependent government as it allows the government to limit its dependence on external borrowing in periods of economic downturn and budgetary shortfall. For instance, in the 2009-10 fiscal year, the government of

Botswana took larger, more stabilization-related withdrawals from the Pula Fund to offset the shortfall in public revenue stemming from the dramatic drop in international diamond demand in late 2008 (International Monetary Fund [IMF], 2010). Since Botswana had managed to accumulate considerable amount of assets prior to the shocks in the diamond market, it was able to rely on international borrowing to a lesser degree than if it had not amassed assets. Since stabilization funds can help minimize a country's dependency on external borrowing, Dixon and Monk (2011, 6) suggest such funds promote financial independence as the country is not subject to the set of conditionalities linked with some external loans.

For stabilization funds' withdrawal and accumulation rules are often guided by a specific projected oil export price or revenue amount. Revenues above this predetermined value are deposited into the stabilization fund, and when oil revenues fall below this value, the distributions from the fund can be used to stabilize the budget. The world oil market is susceptible to temporary and permanent as well as negative and positive price shocks which make it much more difficult to use past resource prices and future resource prices to determine a reliable reference price. However, it is more advantageous for a country to use known data such as previous resource prices rather than unknown data like forecasted future oil prices to determine its resource reference benchmark price (Barnett et al., 2001). Particularly, using a formula containing a long-term moving average of past oil prices is a more objective way to determine the reference benchmark price rather than leaving the resource reference price to the budgetary process which is subject to political motivations (Barnett et al., 2001).

Savings funds for future generations are created to facilitate the optimal utilization of nonrenewable commodities. Fuel and non-fuel mineral wealth are exhaustible resources. Natural resources may be the most valuable, non-human asset that a country possesses and therefore

revenue derived from these finite resources should be prudently invested to yield profitable returns that will remain even after the resources are depleted. According to Heal (2007, 156-170) governments that currently consume their commodity revenues as if they were recurrent income are actually engaged in suboptimal asset disposal; this type of asset disposal only benefits current citizens rather than future generations. Instead revenues should be invested in offshore assets to yield lucrative financial returns and countries can then utilize the dividends as recurrent income. As this stream of public revenue is independent from the fluctuations in commodity markets, it reduces the volatility that commodity-rich governments are exposed to. Also, resource revenues can be set aside to finance capital-intensive, development projects which yield lasting social dividends. By acting as a type of national trust fund, future generation funds or savings funds seek to achieve intergenerational equity in the distribution of benefit from oil wealth or income generated from oil wealth between future citizens and the current generation (Barnett et al, 2001).

Natural resource savings funds generally invest in high-return, long-term assets (low liquidity) as their mandate are to increase the national wealth and their assets do not need to be readily available to stabilize the budget. Similar to stabilization funds, savings funds can also serve as “lenders of last resort;” however, savings funds typically invest in assets with lower liquidity than stabilization funds and therefore their resources are not as readily accessible during periods of budgetary shortfall. Also, future generations funds may have stricter management rules than stabilization funds. According to Fasano (2000, 14-16), the Alaska Permanent Fund and the Kuwait Reserve Fund for Future Generations are two successful savings NRFs and each savings funds has more stringent accumulation rules than its country’s stabilization fund (i.e. the Constitutional Budget Fund for Alaska and the Kuwait General Reserve Fund).

The Political-Economic Rationale for NRFs:

According to Humphreys and Sandbu (2007, 194-195), establishing an SWF (their argument applies mainly to NRFs) is based on a political-economic rationale: by creating an NRF, serious governments hope to change the political incentives that entice current and future leaders to spend oil windfalls prematurely and inefficiently. The authors convincingly assert that a current leader in an oil-rich country is motivated to overspend unanticipated revenue surpluses when he faces high uncertainty about whether he will retain power in the future and/or if he is uncertain whether his successor will maintain his policies and spending preferences (Humphreys and Sandbu, 2007, 199-209). Rather than smoothing expenditure over time, the incumbent is likely to pursue spending-intensive policies when such policies will increase his prospects of retaining power (Humphreys and Sandbu, 2007, 199-209). Moreover, the incumbent leader might be incentivized to overspend, if he can deepen patronage relationships that will be financially advantageous to him after he leaves office (Humphreys and Sandbu, 2007, 199-209). Such an outcome is more likely to occur in societies: (1) where a significant portion of the population is impoverished and have high discount rates; (2) with horizontal¹⁵ and vertical¹⁶ income inequalities where small segments of the society can influence policy and expenditure decisions disproportionately; (3) with few limitations on the government's ability to use funds to expand patronage networks and where citizens are less educated or less aware of the implications of government choices (Humphreys and Sandbu, 2007, 199-209).

Empirical evidence and case studies reveal a weak link between merely establishing a NRF and improved fiscal management (Fasano, 2000; Ross, 2004). Countries and states such as

¹⁵ Horizontal income gap refers to the disparity in income between mineral-rich regions and mineral-poor regions within a country (See chapter 9 by Michael Ross in *Escaping the Resource Curse* for a detailed explanation).

¹⁶ Vertical income gap refers to the gap between the rich and poor populations in a country (See chapter 9 by in *Escaping the Resource Curse* for a detailed explanation).

Norway, Kuwait, Alaska and Botswana who have committed to conservative fiscal policies have also governed their stabilization funds relatively well as evidenced by consistent expenditure smoothing. Nevertheless, their success with expenditure smoothing has been in spite of managing stabilization funds with flexible and at times vague withdrawal and accumulation rules (Fasano, 2000). For example, for the Norway Government Pension Fund-Global (formerly known as the Norwegian Government Petroleum Fund), the government's oil revenues and returns from investments are directly deposited into the fund, however, annual withdrawals are made from the fund to cover the non-oil budget deficit (if there is one) (Skanke, 2003). In the first five years of its operations the Norwegian Fund did not accumulate wealth as the government ran budget deficits to combat the then ongoing recession (Skanke, 2003). Since 1996, the government has ran general budget surpluses and transferred excess revenues to the Fund; consequently by 2012 it had amassed oil revenues and assets worth \$560 billion (Skanke, 2003; SWF Institute, 2012). Norway's success reinforces the fact that a commitment to fiscal discipline whether compelled by clear NRF rules, the general institutional environment in a country or the ideological leans of a particular administration remains key to achieving budget stabilization and expenditure smoothing.

Moreover, disciplined fiscal expenditure has a strong correlation with the strength of institutional checks and balances. Humphreys and Sandbu (2007, 210-212), provide explicit empirical evidence that in countries with weak governmental checks and balances fluctuations in oil revenues lead to changes in public expenditure, especially increases in oil revenues results in upsurges in government consumption. In contrast, in institutionally strong oil producing countries' increases in oil revenues have a minimal effect on government consumption

(Humphreys et al, 2007). One can infer that NRFs, particularly stabilization funds¹⁷ with flexible rules are sustainable in countries that have strong checks and balances since such nations are more likely to manifest the necessary political commitment to pursue budget surpluses than nations that have weak institutional environments. Maintaining an NRF that successfully achieves its savings and/or stabilization mandate in a country with a weak overall institutional environment is less likely than in a nation with generally strong institutional framework. However in a nation with a weak institutional environment, establishing an NRF with a robust institutional design—well-defined accumulation and withdrawal legal rules and strong mechanisms for public accountability and transparency—is more likely to increase the costs to the political leadership for premature spending than an NRF designed with ample discretionary powers. As the political incentives to overspend are altered, expenditure smoothing is more likely to be achieved and fiscal discipline is more likely to be enforced. The institutional set-up and the fund rules for an NRF must be congruent with its national objectives for it to succeed (Monk and Dixon, 2011, 10-11). As shall be seen in chapter three, Nigeria’s management of the Excess Crude Account speaks volumes to this statement.

¹⁷ Fasano shows that savings funds are more likely to be sustainable when they have clear and strict rules as evidenced from the Kuwait Reserve Fund for Future Generations and the Alaskan Permanent Fund.

Chapter 3: The Nigerian Experience with NRFs

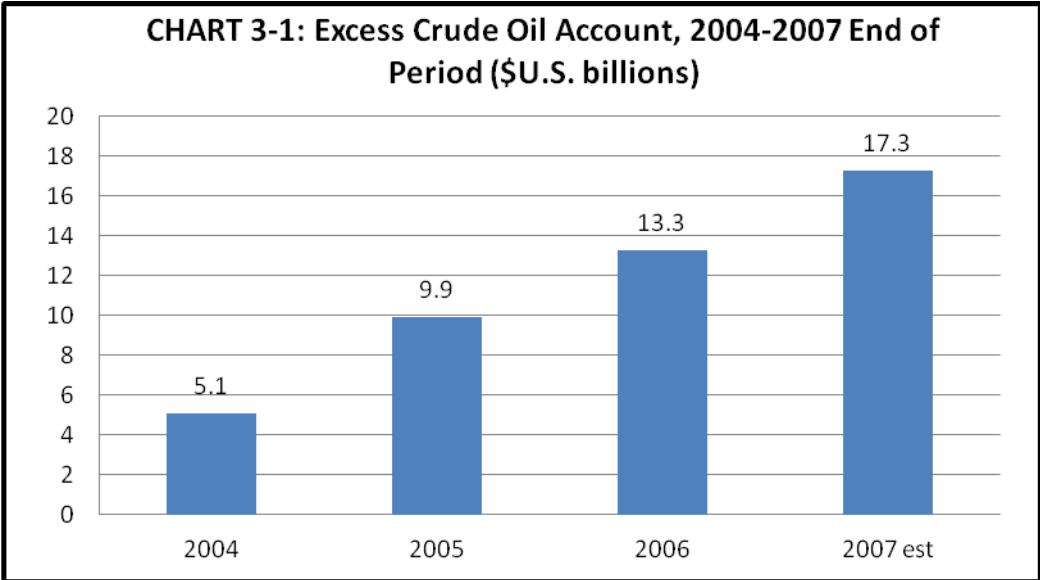
Nigeria has attempted to establish an NRF, specifically a stabilization fund, on three occasions: in 1989, 2004, and 2011 (World Bank, 2003; IMF 2011). More information is available about the second and third attempts which were endeavored after the country's transition to democracy in 1999 than the first attempt under Babangida's military rule. This chapter focuses on the country's more recent attempts to established working NRFs, particularly the Excess Crude Account (ECA) and the NSIA. In the case of the ECA, the chapter chronicles how the incongruence between the fund's fiscal rules and management on one hand and its purported goals compromised its success.

Nigeria's Excess Crude Account: Measurable Success from 2004-2007:

After years of fiscal mismanagement of oil revenues which account for approximately 80 percent of government revenue, Nigeria informally established an NRF in 2004. Ngozi Okonjo-Iweala, Nigeria's current minister of finance, established both the oil budget reference price and the Foreign Excess Crude Account¹⁸ commonly known as the "Excess Crude Account" (ECA) during her first term as finance minister under the second Obasanjo administration (2003-2007). Originally the ECA functioned as a stabilization fund based on an informal political agreement among the three tiers of government rather than with legal backing (Gillies, n.d.; IMF, 2004; IMF, 2005). This informal consensus between the federal government and sub-national governments sidestepped Nigeria's constitutional requirement for revenue-sharing between the three levels of government. The annual oil reference price was determined during the budgetary

¹⁸ Both a Foreign Excess Crude Account and a Domestic Excess Crude Account were created. The Foreign Excess Crude Account had reserves denominated in dollars. The Domestic Excess Crude Account for revenue received from the National Nigerian Petroleum Company and denominated in naira. This paper discusses only on the Foreign Excess Crude Account.

process subject to legislative approval. According to the IMF’s Article IV reports, oil revenues in surplus of the reference price level were deposited in the ECA at the Central Bank of Nigeria (CBN) in the names of the various tiers of government (IMF, 2005; IMF 2011). Between 2004 and 2007, the government accumulated a large balance in the ECA even though the fund was accessed for purposes other than stabilization. In the early years, a conservative oil-based fiscal reference price relative to world market prices was adopted which resulted in significant transfers into the ECA (IMF, 2005).



Source: 2007 IMF Article IV Consultation with Nigeria Staff Report

For instance in 2004, the oil reference price was set at \$25 per barrel while the average oil price was anticipated to be \$33.50 per barrel; this led to a saved surplus of approximately \$6 billion as all tiers of government adhered to the oil-based fiscal reference rule (IMF, 2005). In fact, the savings could have been approximately \$1 billion greater if excess reserves from the domestic sale of oil had also been set aside (IMF 2005). Even as the ECA balance grew, funds were withdrawn from it to pay back the nation’s debt to Paris Club creditors between late 2005 and mid-2006, clearing about 85 percent of Nigeria’s external debt (Okonjo-Iweala, 2008; IMF,

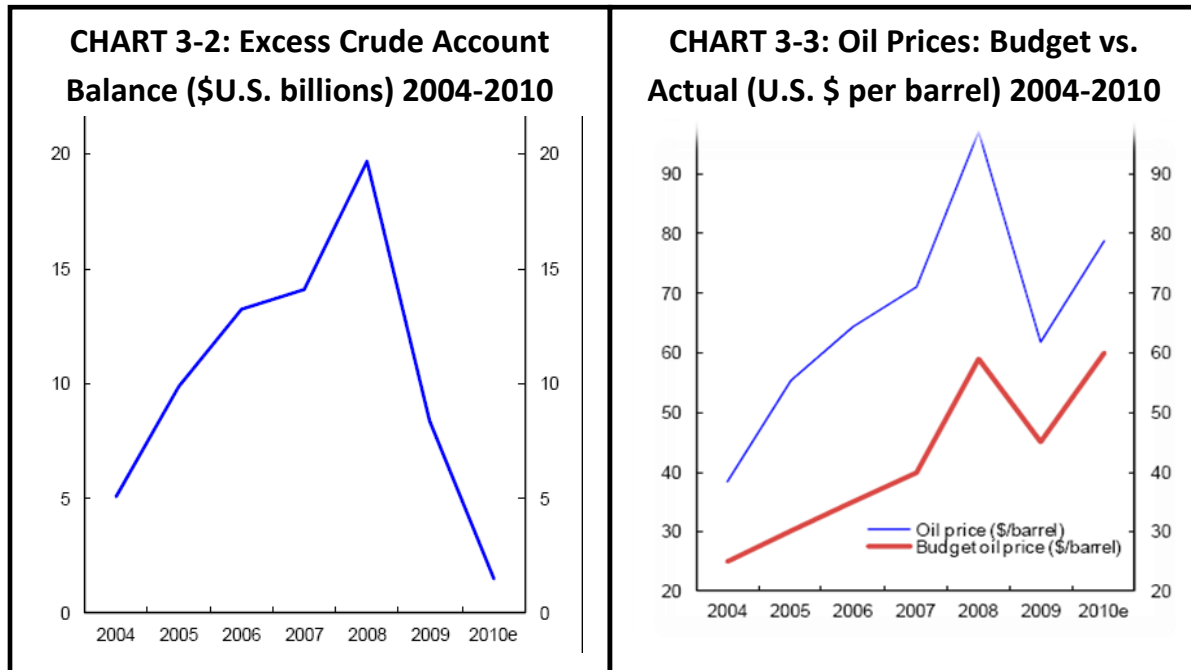
2008; IMF, 2011; Akintunde, 2008). Further withdrawals were made to finance the National Integrated Power Projects, to cover the costs of extending the 2006 national census, and to compensate for budget shortfalls. According to the IMF, the accumulation of surplus oil revenues in the ECA helped to keep public expenditure consistent with the absorptive capacity of the Nigerian economy and contributed to enhanced macroeconomic stability (IMF, 2005).

After years of deadlock in the National Assembly, the Fiscal Responsibility (FR) Act was enacted in mid 2007. Section 7 of the FR Act legitimated the preexisting functions of the ECA. According to the FR Act, the ECA would continue to be housed at the CBN and managed by the CBN governor in consultation with the finance ministers of each government. The FR Act formalized the practice of centralized savings as well as prohibited access to the funds unless the actual reference commodity price fell below the predetermined oil budget reference price for three consecutive months (Fiscal Responsibility Act, 2007). Also, it established the ECA as a capital expenditure fund.

Nigeria's Excess Crude Account: Rapid Decline 2007-Present:

Perhaps, due to the change in leadership as a result of the 2007 presidential, legislative, and gubernatorial elections and the impact of global economic crisis, major political support for the ECA and the provisions for the ECA in the FR Act diminished. Although, some states saw the need to promote national and state-level fiscal responsibility legislation and even create additional state-level savings funds (Gillies, n.d.), several state governors contested their savings being held at the federal level at the CBN as stipulated by the FR Act. Moreover, the ECA suffered from policy coordination problems: clear federal-state communication about the management of the ECA was lacking as many state governors and high level officials were

uncertain whether the CBN was actually providing their states with the payments of interest earned on their share of the ECA funds as required by the FR Act (Gillies, 2009). By late 2007, states were pressuring the federal government for their share of the ECA savings (IMF, 2008). Near the end of that year, an 80/20 rule was proposed whereby 80 percent of all ECA revenues in a given year would be available for disbursement the following year regardless of the FR Act's withdrawal rules (IMF, 2009; IMF 2011). In May 2008, seven states filed a lawsuit against the federal government, seeking their share of revenue accrued from 2004 to 2007 which was placed in the ECA or used by the federal government to pay upfront charges ("Seven states sue FG," 2008; Goitom, 2008). The states withdrew their lawsuit as the federal government agreed to settle the matter through a technical committee of the Federal Accounts Allocation Committee (FAAC) (Mosadomi, 2009). Soon after, the administration of President Yar'Adua (2007-2010) and his successor, Goodluck Jonathan (2010-present), acquiesced to indiscriminate withdrawals from the ECA to appease the states based on the 80/20 rule. (Gillies, n.d.; Mosadomi, 2009; Abubaker and Ahmed, 2010). The implementation of this rule coupled with the sharp fall in world oil prices in late 2008 contributed to a rapid drawdown of the ECA balance from a peak of \$20 billion in January 2009 to approximately \$500 million in August 2010 (Emejo, 2010). The ECA experience clearly illustrates the problems of establishing an NRF without a clear, robust and constitutionally sound framework.



Source: 2009 IMF Article IV Consultation with Nigeria Staff Report

The Recent Legal and Political History of Centralized Savings in Nigeria:

A review of Nigeria’s recent legal history pertaining to revenue-sharing and centralized savings might contextualize some of the weaknesses of the ECA. Nigeria practices fiscal federalism as Section 162 of the 1999 Nigerian Constitution requires that all revenue collected by the federation (except for personal income taxes for military, diplomatic officials, and residents of Abuja) be deposited into the Federation Account (Constitution of the Federal Republic of Nigeria, 1999). All funds in the Federation Account must be distributed among the different tiers of government (federal, state and local) according to a revenue allocation formula determined by the National Assembly (Suberu, 2008). The legislature alters the formula based on proposals submitted by the President on the advice of the Revenue Mobilization Allocation and Fiscal Commission (RMAFC); legislative changes to the formula must remain for at least five years (Suberu, 2008; Constitution of the Federal Republic of Nigeria, Sec). RMAFC is a

committee formed from representatives from each of Nigeria's 36 states and the federal capital territory, with a chairman; it monitors the deposits and disbursements from the Federation Account, and determines the appropriate salaries for the military and political officeholders (Constitution of the Federal Republic of Nigeria, 1999).

Suberu (2008, 465) discloses that at the time of Nigeria's return to democracy in 1999, the National Assembly continued the preexisting military decree for revenue-sharing based on the distribution of 48.50 percent federal government, 24 percent state governments, 20 percent local government councils (LGC), and 7.5 percent special funds. However in the April 2002 verdict of *AG Ogun & Ors v. AG Federation*, the Nigerian Supreme Court declared it unconstitutional for the federal government to divert revenues from the Federation Account to special funds or entities other than the three tiers of government (Suberu, 2008, 466). This ruling invalidated the federal government's statutory practice of allocating 7.5 percent of centrally collected revenues to funds for national ecological emergencies and development. Also, the ruling nullified the federal government's illegal practice of servicing external debts of the federal government directly from the Federation Account before the revenue allocation formula was applied (Suberu, 2008). In subsequent legal cases brought against the federal government by the state governments in 2002, the Supreme Court reinforced the rulings that (1) the Federation Account belonged to all tiers of government, (2) all revenues must be distributed among the three tiers of government, and (3) each government must service its own debt directly from its share of centrally collected revenues (Suberu, 2008, 466-467).

In response to the April 2002 ruling, President Obasanjo unconstitutionally altered the revenue allocation formula, however the Supreme Court upheld his action. Through two executive orders in May and July 2002, President Obasanjo assigned the 7.5 percent that was

previously allocated to special funds exclusively to the federal government (Suberu, 2008). The May 2002 Executive Order designated 56 percent to the federal government, 24 percent state governments, and 20 percent LGCs; the July 2002 Executive Order altered the allocation to 54.68 percent federal government, 24 percent state governments and 20 percent LGCs (Shuaib, 2006). The Supreme Court upheld Obasanjo's modification to the revenue allocation based on Section 315, Subsection 2 of the 1999 Constitution which states that

“an appropriate authority may at any time by order make such modifications in the text of any existing law as the appropriate authority considers necessary or expedient to bring that law into conformity with the provisions of this Constitution” (Constitution, 1999).

In this particular context, the Supreme Court ruled that the federal government and the Obasanjo administration were the appropriate authority to make changes to the revenue allocation principle which is a federal law (Suberu, 2008, 467-468). The Court's ruling in practice shifted constitutional authority to determine revenue-sharing from the legislature to the executive. In 2004, the finance minister revised the vertical¹⁹ revenue allocation to 52.68 percent federal government, 26.72 states, and 20 percent to the LGCs (Shuaib, 2006); the revenue allocation has remained in this configuration since then.

Based on the verdict in *AG Ogun & Ors v. AG Federation*, the ECA was simply illegal from the beginning which explains its vulnerability to political interference despite the passage of the FRA.

¹⁹ Nigeria's fiscal federalism has both a vertical and horizontal component. Vertical revenue allocation formula is between the three tiers of government. In contrast, the horizontal allocation applies only to the states and LGC. Individual states and LGCs receive monies based on the criteria of equality, population, internal revenue, landmass, rural road, inland water way, education, health and potable water. See <http://www.yashuaib.com/formula.htm> for more information.

A Shaky Step in the Right Direction: The Nigerian Sovereign Wealth Investment Authority:

In November 2010, Nigeria's National Economic Council (NEC) (Constitution, 1999), an executive body comprised of the vice president, the 36 state governors and the governor of the CBN approved a plan to replace the ECA with NRFs with legal backing (Ogbu, 2010). The NEC's proposal for an SWF was endorsed by the executive cabinet and introduced into the National Assembly. In mid-May 2011 the Nigerian Sovereign Investment Authority (NSIA) Act was passed by both houses of the legislature (Nwoji, 2011) and signed into law by President Goodluck Jonathan on May 27, 2011 (Nigeria Office of Public Communications, 2008). However, from summer 2011 until about November 2011, the implementation of the NSIA faced serious political and legal opposition from the state governors. In October 2011, over a dozen state governors joined in a law suit to suspend the transfer of US \$1 billion, the initial seed money from the ECA to the NSIA, pending the legal ruling against the federal government for withholding from the states 5.51 trillion naira (US \$ 34.7 billion) which accumulated in the ECA between 2004-2007 through crude oil sales, petroleum profits tax and oil royalties (Songhai Advisory, 2011).

One reason for the loss of political support might be again the change in political office as a result of the April 2011 presidential and gubernatorial elections. Another reason that caused the governors to take a political U-turn might be their rising financial obligations especially due to the passage of the minimum wage act. In March 2011, President Jonathan signed into law a Minimum Wage Amendment Act which increases the minimum wage for all employers from 7,500 naira²⁰ per month as listed in the 2004 Minimum Wage Act to 18,000 naira²¹ per month

²⁰ 7,500 naira is \$47.50 at the current Naira-to-Dollar exchange rate of 157.9 NGN:1USD

²¹ 18,000 naira is \$114 at the current Naira-to-Dollar exchange rate of 157.9 NGN:

(National Minimum Wage Amendment Act, 2011; Folasade-Koyi, 2011).²² Since the new minimum wage will significantly increase the salary burden for state governments, governors want their full share of the revenue allocation rather than save a portion in the NSIA (Ajayi and Olawale, 2011). One can argue that the states' withdrawn support for the NSIA in the face of new fiscal responsibilities is a result of the highly-centralized, "quasi-federalism" (Keller, 2007, 14) that Nigeria has implemented in recent years: the federal government retains the major taxing power of the federation and allocates to itself the lion share of oil revenues (approximately 50 percent after the derivation allocation) (Keller, 2007, 23), while devolving more responsibilities to the states with less resources to fulfill those responsibilities. Additionally, the governors assert that the NSIA Act itself is unconstitutional and it violates the constitutional provision for full revenue-sharing in Nigeria. They threatened to challenge the NSIA's constitutionality in court. In late fall 2011 the federal government and the state governors had reached an out-of-court consensus to go ahead with the establishment of the NSIA with \$1 billion seed money from the ECA and in November 2011, Dr. Okonjo-Iweala revealed that KPMG, a prominent management consultancy and global auditor, had been contracted to recruit the key management positions of the NSIA. KPMG was chosen in order to ensure the transparency of the recruitment process (Walsh, 2011). In late February 2012, the federal government indicated that the NSIA will be fully operational sometime in May 2012 given that the government does not encounter unexpected delays (Aderinokun, 2012). However, the consensus between the federal government and the state governors has broken down again and the Nigerian Supreme Court has stepped in to settle the legal dispute; the court will begin hearing the case on September 25th (Soniya, 2012).

²² National wage is an item on the Exclusive Legislative which means that the federal government has exclusive authority to allocate it.

Major Provisions of the NSIA Act:

With the enactment of the NSIA Act, Nigeria joins 50 other resource-rich nations with SWFs (Nwoji, 2011). The NSIA Act will establish three ring-fenced²³ NRFs: a Future Generations Fund, Stabilization Fund and an Infrastructural Fund, used to invest in infrastructure and transport projects and utility services provisions (IMF, 2010). The NRFs will be initially financed with \$1 billion seed money supplied by all tiers of government and thereafter, in periods of excess oil revenue, each fund will receive 20 percent of oil revenue above the Budgetary Smoothing Amount (Nigerian Sovereign Investment Authority (NSIA) Act, 2010). The Budgetary Smoothing Amount is defined as an amount anywhere between ten percent of monthly projected revenue from non-oil sources up to 2.5 percent of the anticipated annual oil revenue; the Act doesn't specify a particular formula for calculating this amount. (NSIA Act, 2010). The Future Generations Fund and the Infrastructure Fund will continue to receive 20 percent each until they reach a certain percentage of the GDP (NSIA Act, 2010). This percentage will be determined every two years based a to-be-determined actuarial analysis (NSIA Act, 2010).

The NSIA Act (2010) explicitly states that the NSIA will be owned by all tiers of government however, no government in the Federation can borrow against the funds. Also, the NSIA will be an independent entity housed in Abuja, the Federal Capital Territory, with a governing council of owners and board of directors (NSIA Act, 2010). The governing council has a supervisory role and is comprised of the president (represented by the vice-president), the 36 state governors, the minister of finance, the minister of planning, the attorney-general, the CBN governor, the economic advisor to President, four representatives from the private sector, two from Nigerian youth organization, two civil society members and four academics; the

²³ There is no cross-financing between the three funds.

president appoints the non-governmental members with senatorial approval (NSIA Act, 2010; Ekott & Udo, 2011). The board of directors will manage the activities of the NSIA and consists of a chairman, managing director, two executive directors, and a non-managing director who is a legal practitioner, all of whom are appointed by the President (NSIA Act, 2010).

According to Sections 34 and 35 of the Act, based on a unanimous decision by the board of directors and consent by governing council, the NSIA can transfer the uncommitted and un-invested portions of the funds²⁴ from the NSIA to the Federation Account to be distributed based on the ownership shares of each government in the NSIA (NSIA Act, 2010). Also, withdrawals from the NSIA are guided by these conditions (NSIA Act, 2010): (1) There are net profits in each of the funds for at least five years after this Act; (2) each fund has made a net profit in the year of the distribution; (3) the distribution is made after the NSIA determines it can cover all its operational costs; and (4) the distribution must be less than 60 percent of the NSIA's profits in that year.

In the Act, the provision for the management of each fund varies in detail. For instance, the Infrastructure Fund has many explicit rules while the Stabilization Fund has the fewest enumerated provisions. According to the NSIA Act the board will develop a rolling five year investment plan for both the Future Generations Fund and Infrastructure Fund (NSIA Act, 2010). Although the Act states that monies can be withdrawn from the Future Generations Fund, it doesn't provide any stipulations on the use of withdrawn savings. However, Section 42, Subsection 1 stipulates that the Infrastructure Fund can finance development projects in "power generation, distribution and transmission, agriculture, dams, water and sewage treatment and delivery, roads, port, rail and airport facilities and similar assets in order to stimulate the growth and diversification of the Nigerian economy, attract enhanced foreign investment and create jobs

²⁴ The NSIA Act doesn't clearly specify which of the three funds.

for Nigerians” (NSIA Act, 2010). Also, the Infrastructure Fund will “be able to make private equity investments in reputable firms involved in infrastructure activities, co-invest directly in infrastructure projects, and participate in infrastructure funds with multiple outside investors” (IMF, 2011, 34). The NSIA has the right to determine the viability and financial returns of projects proposed by the various levels of government in the federation. Specifically, the NSIA can delegate the National Economic Council to establish a committee to assess the viability of the proposed projects or employ a private asset manager to perform the task (NSIA Act, 2010). Also, the Infrastructure Fund can investment up to 10 percent of its monies into development projects that promote economic development in underserved sectors or regions which present a less favorable economic return (NSIA Act, 2010). Lastly, at the request of the finance minister, the NSIA will release monies from the Stabilization Fund to cover the difference between the anticipated oil revenue amount and (the lower than anticipated) actual amount received that quarter. Like other SWFs, the NSIA is able to create subsidiaries which are able to issue bonds and incur debt subject to the approval of the Minister of Finance (NSIA Act, 2010).

Nigeria has had a less than stellar track record with establishing and managing NRFs. The NSIA Act was proposed to address some of the major shortcomings of the ECA and provide a clear legal backing for centralized savings and investment; however the NSIA Act is at best a modest improvement over the ECA. In the following chapter, I will provide an assessment of the NSIA Act’s strengths and weaknesses and offer recommendations on how to better safeguard the NSIA from political interference and to enhance public accountability of the NSIA.

Chapter 4: The Strengths and Weaknesses of the NSIA Act and Recommendations

In this chapter, I address the major strengths and weaknesses of the NSIA Act. The Act's shortcomings are classified into three broad categories, and recommendations are provided under each category. These recommendations hope to strengthen the NSIA's institutional effectiveness and sustainability so that it overcomes the problems that plagued the ECA.

Strengths of the NSIA Act:

The NSIA Act was proposed to address some of the major shortcomings of the ECA and provide a clear legal backing for centralized savings and investment; it achieves this goal in some respects. First, the NSIA Act clarifies the issue of ownership of the three funds better than the former FR Act did for the ECA. The Act sets clearer limitations for ownership by stating that all tiers of government will own the NSIA but that no government can access the funds without approval from the NSIA Board. The elucidation of what ownership entails is particularly important because prior to the passage of the FR Act, it was unclear which tier of government owned the ECA in practice and if ownership guaranteed access to the ECA funds. From 2004 to 2007, the federal government withdrew monies from the ECA to finance its own goals (not related to budget stabilization) and it was ambiguous if the states had legal right to use the ECA's revenues. In 2009, the states, asserting their claim to revenue-sharing, reached an agreement with the federal government whereby the majority of funds from the ECA would be divvied up among the different tiers of government.

Moreover, the NSIA will be aided by its institutional separateness: the funds will not be housed at the CBN or managed by the CBN governor. Previously, the sub-national governments had contested the CBN's management of their share of the federation's savings in the ECA.

Additionally, section 32 prohibits any government of the federation from borrowing against the NSIA funds, (NSIA Act, 2010). This prohibition against borrowing was not in the FRA and will help defend the three funds from the potential fiscal indiscipline (Goitom, 2011).

Furthermore, the Act stipulates robust reporting, auditing and conflict of interest provisions, thus promoting greater accountability and transparency in the fund management. The NSIA Act requires annual internal and external audits according to International Financial Reporting Standards (NSIA Act, 2011). Additionally, section 27 requires that the remunerations of board members must be included in the publicly accessible, annual reports. Members of the board are required to disclose any conflict of interest that they may have and these issues must be documented in the minutes of the board meetings. Under the section of the Act titled “supplementary provisions relating to the board,” all board members and employees of the NSIA are prohibited from purchasing assets of the NSIA in a “personal capacity;” however the interpretation of the term, “personal capacity” is ambiguous (NSIA Act, 2011). Additionally, as the NSIA is classified as a “public institution” under the definition offered in the Nigeria’s 2011 Freedom of Information (FI) Act, it is required to abide by the transparency provisions outlined in the FI Act (FI Act, 2011).

Finally, the version of the NSIA Act that was enactment requires that presidential appointments to the governing council must be approved by the senate (Ekott & Udo, 2011). Hopefully, this provision will constrain the president to appointing individuals to the governing council who are committed to maintaining the NSIA’s institutional independence and integrity.

Shortcomings of NSIA Act and Clear Recommendations:

Despite these improvements from the ECA, the NSIA Act has numerous and serious shortcomings. These shortcomings may jeopardize the sustainability of the three NRFs and the institutional independence of the NSIA as the current Act doesn't effectively alter the political incentives that leaders have to overspend. This is particularly disconcerting as Nigeria has a history of inefficient and premature spending of oil windfalls and a robust NSIA Act is critical to achieving the NSIA's mandates. The following shortcomings raised are categorized based on whether they 1) point out NSIA's dubious constitutional stance 2) highlight potential fiscal policy coordination problems, 3) fail to appropriate constraints on the NSIA's resources and 4) may produce gaps in the transparent and accountable management of the NSIA. The recommendations offered aim to address the unique political economy issues of Nigeria in these four areas and to strengthen the NSIA.

1. The NSIA's Questionable Constitutionality:

It is unclear if the NSIA Act is constitutional. First, it does not address the issue of centralized savings and revenue allocation in line the 2002 Supreme Court verdicts of *AG Ogun & Ors v. AG Federation* and *AG Cross River vs. AG Federation & Another*. The Supreme Court ruled that all centrally-collected revenues from the federal government must be deposited into the Federation Account to be divvied up among the three tiers of government; the court invalidated special accounts financed by direct withdrawals from the Federation Account (Suberu, 2008). At the time of NSIA's enactment in May 2011, the Act shared the support of the state governors. However since then, the state governors have continually challenged the NSIA's constitutionality and even filed a lawsuit in October 2011, only to succumb to the federal

government's request to settle out of court; however, these settlements have been short-lived and a legal recourse has resumed (Songhai Advisory, 2011; Soniyi, 2011).

Nevertheless, federal government asserts that the NSIA is already constitutional and that centralized savings can be legally interpreted in a manner that is constitutionally sound. The federal government makes three legal arguments: First, centralized savings "may be regarded as promoting a system of deferred distribution of a portion of the Federation Account, which may not necessarily be in conflict with Section 162 of the Constitution" (Yusuf, 2011). By this, the federal government asserts that each state government is not permanently denied its share of oil revenues saved in the NSIA as each state's share will be distributed to it during periods of revenue shortfall. Last summer, I had the opportunity to speak with one of the legal consultant who advised the federal government during the drafting of the NSIA legislation. The consultant reiterated the federal government's first legal argument, but also claimed that the withdrawals from the Infrastructure Fund will not be guided by the revenue allocation formula but by other criteria. Although "deferred distribution" may be appropriate for revenues transferred into the Stabilization Fund, it is simply unclear how this argument will apply to states' portions allocated to the Infrastructure Fund and Future Generations Fund. Perhaps, these two funds will be exempt from revenue-sharing under the federal government's second legal argument: the federal government alleges that the NSIA legislation is consistent with Section 162, Subsection 3 which empowers the National Assembly to determine the "terms" and "manner" in which revenue may be distributed between the different tiers of government (Constitution of Nigeria, 1999). The National Assembly in enacting the NSIA Act only determined the "terms" and manner" for revenue-sharing. Thirdly, although NSIA and

centralized savings does not fall under the exclusive legislative list²⁵ or concurrent legislative list,²⁶ the federal government's attorney general argues that the economic objectives of the NSIA, outlined in Section 3 of the Act are consistent with the economic objectives of the "state" provided in Section 16 and thus the NSIA is constitutional (Constitution of Nigeria, 1999; Yusuf, 2011). One thing that remains unclear is whether the word "state" in this provision refers to the federal government, the state governments or both. Nevertheless, the federal government appears committed to the NSIA and its current constitutional legitimacy based on these legal grounds.

However, since the May 2011 enactment and the aftermath of the 2011 elections, many state governors have alleged that the NSIA Act is unconstitutional and rescinded their support for the NSIA's establishment. Specifically, the governors view the NSIA as an illegal confiscation of a portion of their share of oil monies and in direct violation of Section 162 and fiscal federalism (Songhai Advisory, 2011). Moreover, some states have argued that centralized savings isn't necessary and that the state governments should receive all their revenue allocation and establish individual NRFs at the state level. However, centralized savings rather than state level NRFs may be more suitable for Nigeria for several reasons. First, if SWFs are managed at the national level, then oil revenues can be pooled to achieve national objectives that benefit all states or address the inequities between states. Second, centralized savings funds can be used to finance development projects in less developed regions or states which may receive a smaller percentage of the revenue allocation formula and thus would not be able to fund necessary development plans on their own. Third, having sub-national funds in place of a centralized

²⁵ The Exclusive Legislative List refers to the lists of matters that the National Assembly has the sole constitutional authority to pass legislation on, to the exclusion of the State Assemblies.

²⁶ The Concurrent Legislative List refers to the list of items that both the National Assembly and State Assembly have exercisable power.

savings scheme does not mitigate the problem of macroeconomic volatility for states as the need to save would be the prerogative of each state.

The constitutionality of the NSIA is a matter for the Nigerian Supreme Court to decide in line with its jurisprudence on fiscal federalism. If the NSIA's constitutional soundness is not decided in Court, then the NSIA's sustainability will rely on the strength of the political deals cut between the state governors and the federal government, which from previous experiences appear to be shaky agreements.

2. The Need for Clear, Specific Fund Rules:

In the case of Nigeria, the Act's fund rules, i.e. provisions for determining the oil-revenue reference price, deposits, withdrawals and spending priorities, may not adequately buffer the NSIA from the country's political-economic incentives to overspend due to economic downturns, fiscal federalism, and entrenched patronage networks. First, a clear principle for determining the oil-revenue reference price such as the long-term moving average of past oil prices principle is not enshrined in law but is determined annually by the president during the budgetary process subject to the approval of the legislature. This is particularly problematic since in the past Nigeria's oil reference price has been changed during the budgetary/ appropriations process (IMF, 2011). For instance, the executive branch proposed an oil benchmark price of \$65 per barrel for 2011-2013, however in the passing the 2011 Budget Appropriation Act, the National Assembly raised the oil benchmark price to \$75 per barrel (IMF 2010; Nzeshi, 2011). If the oil revenue benchmark price is consistently set unrealistically high, a reduced amount of revenue will be deposited into the NRFs in the first place and the Stabilization Fund will be drawn down to its limits more often. The International Monetary Fund projects that Nigeria can

save approximately up to \$40 billion in oil revenues from 2011-2013, however this might not happen if the oil benchmark price is continually changed by the political process (IMF, 2011).

Moreover, the NSF's' withdrawal rules provided in the NSIA Act are too broad and unclear. Section 34 and 35 of the Act which outline the general withdrawal rules for the NRFs are an improvement from the ECA as rules require that monies held by the NSIA cannot be accessed for at least five years after the enactment of the NSIA Act. If future oil prices are as high as anticipated, and if the NSIA becomes operational and this provision is adequately implemented, the NSIA will shores up substantial savings for at least the next few years. Yet, the withdrawal rules are still vague, leaving significant discretionary power to both political actors and the NSIA to determine how to implement these rules. For instance, section 35 requires the governing council to approve of the board's withdrawal decisions before disbursements can be made. However, the Act does not stipulate the level of approval—whether a majority or a unanimous approval—is needed by the governing council. Moreover, section 47 gives the NSIA the right to abide by requests from the minister of finance for disbursement from the Stabilization Fund. Nonetheless, according to the language of section 48 when the finance minister at the end of any financial quarter requests that the NSIA withdraw monies from the Stabilization Fund to cover the difference between the anticipated and actual federation revenue, the NSIA is obligated to fulfill the request. It's unclear who has the final authority to release monies from the Stabilization Fund. Additionally, the Act doesn't specify conditionalities for withdrawals from the Future Generations Fund or evaluative requirements to assess whether the disbursements were used efficiently. Lastly, there are no explicit procedural mechanisms for withdrawals (i.e. withdraws must be done as electronic transfers) to ensure that disbursements are diverted to the approved purposes.

Having vague fund rules is not uncommon among NRFs; in fact NRFs such as Botswana's Pula Fund have been successfully managed despite their vague rules. However, for a country like Nigeria which struggles with systemic corruption, vague rules may result in misappropriated monies. NSIA would benefit from clearer rules such as legally enshrined, qualitative earmarks on how NRF resources can be spent (Humphrey et al, 2007). For instance, the Alaska Permanent Fund (APF)'s requirement that 50 percent of the APF's investment returns be distributed to eligible Alaskans while the remainder must be used first to inflation-proof the principle (Humphrey et al, 2007; Fasano, 2000). In addition to qualitative restrictions, robust quantitative rules which state an explicit formula or percentage of the NRF's resources that can be withdrawn over a given period will limit the government's discretionary powers relating to expenditure; a more constrained government will more likely depoliticize withdrawals from an NRF. Ideally, the NSIA Act should be amended as these rules should carry a legal mandate.

3. The Need to Coordinate Spending Outlays from the Infrastructural Fund with Fiscal Priorities:

Additionally, there is no clear fiscal policy coordination on how the Infrastructure Fund will be coordinated with the government budget to mitigate macroeconomic volatility. Section 42, Subsection 1 asserts that investments from the Infrastructure Fund must be congruent with the "infrastructure priorities and plans developed by the appropriate ministries and agencies with responsibility over the particular infrastructure asset sector" (NSIA Act, 2010). This provision does not specify mechanisms by which the NSIA coordinates its approved development projects with government budgets so as to avoid overlapping capital expenditure. To address this issue, the NSIA Act could be amended to require that development projects tabled before the Fund

must be explicitly congruent with the specific capital allocation priorities outlined in the country's medium-term expenditure framework (MTEF) before they can be approved for financing from the Infrastructure Fund. Such a provision would reinforce the federal government's commitment to prudent fiscal management as outlined in the 2007 FRA and incentivize states to pursue better fiscal policies. Also, this additional stipulation will reduce the possibility of overlapping expenditures and lead to more accurate depiction of the amount of public revenues spent on development throughout the federation (DiLorenzo, 1985).

Alternatively, the MTEF can be established independent of the Infrastructure Fund's five year investment plan (in terms of investments in physical infrastructure and not financial instruments), and then NSIA's management board, key federal ministers should meet to harmonize the two plans. Once the initial financing of projects has been completed, and now these capital spending outlays become recurrent expenditures, the policy coordination between the NSIA and key ministers is essential to ensure that government ministries can accommodate the increased recurrent expenditures.

4. Provide Legal Standing to Promote Accountability:

Finally, to strengthen the NSIA and just as it is stipulated in the FR Act, the NSIA Act could empower Nigerian citizens with the legal standing to sue the federal government if need be, in order to ensure that the provisions of this Act are implemented. This recommendation is consistent with Nigeria's 2011 FI Act which provides Nigerians access to public records and institutions. Since the Nigerian people are the beneficiaries of these NRFs, especially the Future Generations Fund, it seems appropriate that they should be able to ensure that *their* national wealth is well-managed. Giving explicit legal standing to Nigerian citizens may alleviate some of

the principal-agent monitoring problems associated with mineral wealth revenue management. Additionally, Nigerians have demonstrated a commitment to use legal measures to compel action from their government. In 2009, the late President Yar'Adua left the country indefinitely to receive medical treatment in Saudi Arabia without formally handing over power to his Vice President, Goodluck Jonathan. This resulted in a leadership vacuum. In response, the Nigerian Bar Association sued the federal government in Federal High Court to compel the federal executive cabinet to begin the process of handing over power to then-Vice President Jonathan in a manner consistent with the constitution (Anon., 2010). Although, the Federal High Court ruled against the Nigerian Bar Association, the political frenzy of the situation motivated the Senate to legally (albeit unconstitutionally) empower Mr. Jonathan as the Acting President. Given Nigeria's history, empowering citizens with legal standing does not guarantee that the best legal outcome will be undertaken, but it is more likely to nudge the government out of a position of political inertia and in the right direction. Overall, if these recommendations are implemented, they will give the NSIA Act the teeth it needs to protect the three NRFs from political interference which was the major pitfall of the ECA.

Implementing a more robust NSIA Act is only one initiative among many that the Nigerian government would need to commit to ensure the prudent utilization of its oil assets to generate sustainable income and tangible public goods for its citizens. Ideally, Nigeria must reevaluate and restructure the various stages of its extractive industries value chain²⁷ in ways that foster transparency, strengthens governance structures, and promotes economic and environmentally-friendly development. The conclusion offers a more pragmatic approach to achieving the first step in improved oil revenue management.

²⁷See http://siteresources.worldbank.org/INTOGMC/Resources/ei_for_development_3.pdf for an overview of the extractive industries value chain.

Conclusion: Small, Realistic Steps toward Improved Oil Revenue Management

In this analysis, I began with an examination of Nigeria's oil revenue management history, illustrating the distinct challenges that the country has faced in managing its natural resources and unfortunately how it has poorly managed them. Chapter two provided an overview of sovereign wealth funds and with a particular emphasis on NRFs as a tool to address the fiscal, macroeconomic and political challenges associated with being a resource dependent country. Building from an understanding of Nigeria's history and natural resource funds in general, chapter three offered an analysis of Nigeria's recent experiences with NRFs since 2004 as well as a detailed summary of the 2011 NSIA Act. The NSIA Act is a welcomed improvement from the ECA and the FRA which attempted to legalize it. However, along with its strengths, there were serious weaknesses in the legislation which I discussed in chapter four.

Ideally, oil revenue management reform (ensuring the NSIA success) in Nigeria should be an integrated process that is linked to increasing transparency in oil contracts, commercializing the Nigerian National Petroleum Corporation (NNPC), implementing Nigerian Extractive Industries Transparency Initiative (NEITI) audits among other institutional and legislative reforms. Comprehensive reform of this nature is difficult to orchestrate. Yet, the NSIA can still be a small but notable fixture of good governance among Nigerian's weak institutions. This idea of having a functioning institution in the midst of weak, corrupt institutions echoes the concept of "small-g" governance.

Big-g Governance vs. Small-g Governance:

In "The Case for Principled Agnosticism," Brian Levy (2010), former head of the Governance and Anti-Corruption Secretariat at the World Bank Group offers an evolutionary

framework to understand how developing countries can transition to economically developed, stable democracies with strong institutions. The aim of the evolutionary approach is “to nudge the [institutional] system” of a country so that that in ten years the country’s development and governance prospects in at least some but not all areas have improved from the outset (Levy, 2010).

Also, Levy distinguishes between two types of governance reform initiatives that development practitioners can take. The first, he calls “big-g” governance reform which refers to the “strengthening of national-level institutions that hold government to account” (Levy, 2010, 30). He (2010) argues that past development programs have implemented predominately “big-g” governance reform but with lackluster success because these types of reform are encumbered by the local politics of the country. Its counterpart is “small-g” governance reform, which he refers to as reforms that engender “participation in and oversight of the provision of public services by stakeholders with strong, unambiguous incentives to achieve good results” (Levy, 2010, 30). Greater community supervision of local health clinics or road-maintenance projects may be an example of this. Levy advocates that development practitioners harness opportunities to achieve “small-g” governance initiatives as these types of reforms are easier to achieve, and lead to incremental changes that may cumulatively create the environment for future “big-g” governance reforms to prosper.

Small-g Governance to Big-g Governance in Efforts to Strengthen the NSIA:

Levy’s concept of small-g governance providing the measurable changes needed for big-g governance can be applied to strengthening the NSIA in two sequential ways: 1) in building awareness for centralized savings in Nigeria among both civil society actors and average

citizens; 2) in mobilizing this constituency to push for major changes to the NSIA Act and greater accountability. Both of these steps are needed to achieve more meaningful change in Nigeria.

As I have conducted research on the NSIA Act and the publicized political situation surrounding it, I have noticed that a major category of stakeholders are absent from the dialogue. The perspectives of Nigerian governments (both the federal and state governments officials) and international and local policy analysts have dominated the debate, followed by the World Bank, and a few Nigerian economic policy and governance organizations asserting their opinions. But, the voices of Nigerians citizens have not been heard. I have only come across one editorial piece that sought the opinion of a Nigerian citizen on the NSIA. Perhaps, the Nigerian public is not aware of the NSIA Act or not interested in it. Sensitizing Nigerians, particularly the youth as they are the country's largest demographic group, and greater number of civil society organizations about the NSIA is the first step. Nigerian youth should be informed on what the NSIA is, how it will operate, and most importantly how a properly functioning NSIA can tangible benefit them. Institutions like the Nigerian Federal Ministry of Youth Development and Nigerian, youth-centered, leadership organizations such as the Youngstars Foundation²⁸ or the Guardians of the Nation International (GOTNI)²⁹ (just to name a few) should engage with Ministry of Finance³⁰ to answer questions such as: in what specific ways can revenues from the Future Generations Fund be used to benefit the Nigerian youth? As Nigeria's botched oil subsidy removal early this year has shown, government policies will fail without the legitimate backing of the general public. Educating the public, particularly the youth about the NSIA and

²⁸ Visit <http://youngstarsfoundation.org/> to learn more about the Youngstars Foundation.

²⁹ Visit <http://www.gotni.org.ng/gotni.org.ng/> to learn more about GOTNI.

³⁰ Until the NSIA becomes operational, the Ministry of Finance appears to be taking the lead on sovereign wealth fund management in Nigeria.

acknowledging them as key stakeholders will engender the long-term public backing that the NSIA needs to succeed.

Moreover, educating the public and widening the group of civil society organizations involved, will create a group that can be mobilized to push for “big-g governance” reforms that can enhance the NSIA’s sustainability. “Big-g governance” initiatives are reforms that will create political winners and losers, are more difficult to build a consensus for, and will enhance the institutional capacity of the NSIA. Determining the constitutionality of the NSIA is the most salient “big-g governance,” initiative for the NSIA. Civil society organizations can be mobilized to push for the Supreme Court to evaluate the constitutionality of the NSIA without delay. If the federal government’s argument for centralized savings schemes like the NSIA is upheld by the Supreme Court (i.e. the federal government “wins” and state governors “lose”), then the NSIA will be more shielded from future demands for indiscriminate withdrawals based on the principle of revenue sharing. However, if the Supreme Court deems that the NSIA is unconstitutional (i.e. the federal government “loses” and state governors “win”), then, the National Assembly can, if desired, take the necessary steps to write a constitutionally sound NRF law or amend the constitution. It is better for the federal government to be assured of the NSIA’s constitutional soundness, than to operate the NSIA based on an informal and shaky political agreement with the state governors, an agreement that has a high risk of failure. The second “big-g governance” reform³¹ is establishing clear fund rules especially withdrawal and spending rules guiding the management of the Future Generations Fund. It is essential that civil society organizations and the public are involved in this process of determining how saved revenues can be earmarked for certain development initiatives since in theory, the Nigerian public is the ultimate beneficiary of such resources. Whether the inclusion of civil society in creating the Future Generations Fund

³¹ The second “big-g governance” reform is contingent on if the NSIA is found constitutional.

rules occurs in an amendment process of the current NSIA Act or during the drafting of a new NRF legislation depends on whether the Supreme Court determines that the NSIA Act is constitutional or not.

By educating the Nigerian public and civil society groups, (i.e. a key group of stakeholders) a constituency group for the NSIA will coalesce which can then be mobilized to pursue reforms that are vital to the NSIA's sustainability. As the federal government has pursued an independent process to hiring the NSIA's management board, the NSIA (as of now) appears not be engulfed by internal, entrenched political actors who oppose responsible oil revenue management (Walsh, 2011). Therefore, these small-g and big-g governance initiatives are more likely to produce meaningful change in at least one public institution managing the country's oil revenues. These changes may over time engender the political environment (in terms of momentum, invested constituency groups, and political will) needed for substantive institutional reform to succeed in other public institutions that currently have political actors diluting reform initiatives. Perhaps, a properly functioning NSIA can "nudge" Nigeria's revenue management system forward such that ten years from now, the country's prospects are a bit brighter.

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