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FISCAL POLICY OPERATIONS AND EXTERNAL TRADE DYNAMICS: RELEVANCE TO FINANCIAL EDUCATION IN NIGERIA

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ABSTRACT

This study investigates how fiscal policy operationsdisaggregatedinto government capital expenditure (GCE), government recurrent expenditure (GRE), and deficit financial management (DFM) affect Nigeria's foreign-trade performance (trade intensity) over 1990–2024 using ARDL bounds testing, ADF unit-root tests and error-correction estimation. The results show a stable long-run relationship between trade intensity and fiscal operational variables, with GCE exerting a positive and significant long-run effect, GRE showing an insignificant long-run effect, and deficit financing gap exerting a negative and statistically significant short-run effect. The findings imply that fiscal composition and financing modalities matter more than headline spending: sustained public capital investment supports trade performance, while deficits and poorly targeted recurrent spending undermine it. Policy recommendations include prioritizing trade-enabling public investment education, improving public investment management and project readiness, reorienting recurrent spending toward trade-supporting services, and strengthening revenue mobilization and promoting deficit financing education.

KEYWORDS: - Fiscal Policy, Trade Intensity, Government Capital Expenditure, Fiscal Deficit, Trade Openness.

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Volume 4 Issue 4, July-August 2026, pp 117-128

1.0 INTRODUCTION

Foreign trade is a core engine of economic development. It supplies foreign exchange, widens markets for domestic producers, and accelerates structural transformation by linking firms to larger, more competitive markets (Nwagu et al., 2022; Jones et al., 2025). Exports finance the import of capital goods and intermediate inputs that raise domestic productivity, while imports provide inputs and technologies that support value-added production; together these flows shape employment, investment and macroeconomic stability (Yusuf & Magaji, 2023; Onuchuku&Obayori, 2018). For developing economies such as Nigeria, a deeper and more diversified export base reduces vulnerability to commodity shocks, strengthens reserve buffers and creates fiscal space for public investment.

Nigeria's trade record over recent decades has been shaped by oil dependence, exchange-rate volatility and episodic policy shifts, producing a volatile pattern of trade balances and a persistently weak non-oil export sector (Odungweru&Ewubare, 2020; Nwagu et al., 2022). Time-series and cointegration studies find long-run links between macro policy variables and trade flows, but report mixed short-run effects: money supply and exchange-rate movements frequently matter for export and import dynamics, while fiscal variables show heterogeneous impacts depending on whether spending is capital-oriented or recurrent and on how deficits are financed (Ashamu, 2020; Yusuf & Magaji, 2023). Furthermore, it is evident thatproductive public investment and improved trade facilitation are associated with better balance-of-payments outcomes, whereas high recurrent spending, distortive taxation and weak project implementation blunt the trade benefits of fiscal outlays (Onuchuku&Obayori, 2018; Onwe & Okoro, 2015; Jones et al., 2025).

Fiscal policy, which refers to government choices over taxation, public spending (recurrent versus capital) and borrowing, is crucial to foreign trade through multiple, interacting channels. Public capital spending on ports, roads, power and trade-facilitating infrastructure lowers trade costs and raises exporters' supply capacity, while tax and tariff settings change relative prices and firms' export margins; conversely, large deficits and the mode of deficit financing (monetization or external borrowing) influence interest rates, the real exchange rate and private investment, with direct consequences for import demand and export competitiveness (Onuchuku&Obayori, 2018; Onwe & Okoro, 2015; Nwagu et al., 2022). Evidence from literature showsthat well-targeted capital expenditure and trade-friendly tax measures are associated with improvements in balance-of-payments indicators, whereas recurrent-heavy budgets, poorly designed tax regimes, and fiscal actions that are effectively monetized tend to widen import demand and erode competitiveness (Onwe & Okoro, 2015; Eze & Eze, 2020; Yusuf & Magaji, 2023).

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

Despite a growing body of time-series and cointegration studies on Nigeria's external sector, findings remain mixed and important gaps persist as regards the role of fiscal policy. Some find that government capital spending improves external balances (Onuchuku&Obayori, 2018), while others report that aggregate government expenditure or taxation can depress non-oil exports (Onwe & Okoro, 2015). These inconsistencies trigger some policy-relevant questions: Whichfiscal instruments reliably raise non-oil exports? How does the financing mode alter trade outcomes? Which remain insufficiently answered in the Nigerian context.Filling these gaps is urgent for Nigeria's macroeconomic stability and diversification agenda.

The country's heavy reliance on oil receipts, recurrent exchange-rate volatility and episodic fiscal stress mean that poorly designed fiscal actions can quickly translate into import surges, reserve losses and weakened export competitiveness; conversely, well-sequenced capital spending and export-friendly tax reforms can strengthen the non-oil tradable base and create fiscal space (Onuchuku&Obayori, 2018; Onwe & Okoro, 2015; Nwagu et al., 2022).

This study, therefore, disaggregates fiscal composition, models financing channels, and uses recent post-2015 data to identify causal effects which would provide financial literacy evidence for policymakers in order to educate andclarify which fiscal operators raise export capacity. Such evidence is essential to move beyond headline spending targets toward fiscal strategies that reliably convert public resources into durable, trade-enabling assets and measurable improvements in Nigeria's external position.

2.0 LITERATURE REVIEW

Fiscal policy is a multifaceted concept that scholars and institutions define in ways that reflect both theoretical emphasis and operational practice. At its broadest, economists describe fiscal policy as the government's deliberate use of taxation, public expenditure and borrowing to influence aggregate demand, allocate resources and shape the distribution of income (Yusuf & Magaji, 2023; Nwagu et al., 2022). Horton and El-Ganainy (2019) assert that "fiscal policy is the use of government spending and taxation to influence the economy". They further stressed that "governments typically use fiscal policy to promote strong and sustainable growth and reduce poverty".

Keynesian scholarship highlights fiscal policy's role in demand managementusing spending and tax changes to stabilize output and employment, while public-finance literature focuses on how tax design, public investment and debt management affect incentives, long-run growth and intergenerational equity. Monetarist and classical perspectives, by contrast, treat fiscal actions as interacting with monetary conditions and supply-side fundamentals; in applied work these theoretical strands converge on a practical menu of instruments (public capital versus recurrent

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

spending, tax bases and rates, subsidies, and the composition of borrowing) because those are the levers that directly alter prices, returns and cash flows in the economy (Nwagu et al., 2022; Yusuf & Magaji, 2023)

In developing economies, such as Nigeria, the definition is usefully narrowed to a handful of instruments that directly affect trade-enabling activity: public capital expenditure (PCE)thebudget lines that finance roads, ports, power, water and public buildings and thereby create immediate demand for contractors and inputs (Onuchuku&Obayori, 2018; Ojo et al., 2023); gross fixed capital formation (GCF), which captures the total investment in physical assets and thus reflects both public and private construction and logistics capacity (Ojo et al., 2023; Okeke, 2023); tax and tariff policy, which both funds public investment and alters firms' incentives and effective costs through corporate taxes, VAT, import duties and compliance regimes (Onwe & Okoro, 2015; Eze & Eze, 2020); and deficit financing and debt management, where the choice between domestic monetization, domestic bond finance and external borrowing affects interest rates, crowding-out risks and the sustainability of fiscal support for trade infrastructure (Debt Management Office, 2018; Nwagu et al., 2022).

Foreign trade refers to the exchange of goods, services, and capital across national borders, enabling countries to access products they do not produce efficiently and to sell their own output in global markets. It is widely regarded as a catalyst for economic growth because it expands market size, enhances specialization, facilitates technology transfer, and generates foreign exchange earnings that support macroeconomic stability (Frankel & Romer, 1999, as cited in Nwagu et al., 2022; Jones et al., 2025). Foreign trade is also viewed as a mechanism for structural transformation: by integrating into global value chains, countries can diversify away from primary commodities, upgrade production capabilities, and stimulate investment in tradable sectors (Usman & Yusuf, 2023).

For open economies like Nigeria, foreign trade plays a dual role, supporting domestic production through the importation of intermediate and capital goods, and contributing to national income through export revenues. The literature consistently emphasizes that the effectiveness of foreign trade depends on macroeconomic policies, especially fiscal and monetary policies, which shape competitiveness, production costs, and the overall trade environment (Nwagu et al., 2022; Onuchuku&Obayori, 2018). In particular, fiscal instruments such as public investment, taxation, and tariff structures influence the cost of doing business and the capacity of firms to participate in global markets (Onwe & Okoro, 2015). Moreover, the stability and credibility of macroeconomic policy frameworks determine investor confidence, exchange-rate dynamics, and the ability of domestic producers to integrate into international value chains (Yusuf & Magaji,

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

2023). These factors underscore that foreign trade outcomes are not solely market-driven but are deeply embedded in the quality and orientation of a country's fiscal policy stance.

Foreign trade performance is typically assessed using several quantitative indicators that capture the scale, direction, and balance of a country's external transactions. The most common measure is the trade balance, defined as the difference between the value of exports and imports; a surplus indicates that export earnings exceed import payments, while a deficit reflects the opposite (Onuchuku&Obayori, 2018). Another key measure is net exports, which form part of the national income identity and reflect the contribution of external trade to GDP (Eze & Eze, 2020). Broader assessments use the balance of payments (BOP), a comprehensive record of all economic transactions between residents and the rest of the world, including the current account (trade in goods and services, income flows) and the capital and financial accounts (Onuchuku&Obayori, 2018). Additional indicators include export diversification indices, which capture the degree of concentration in export products; terms of trade, which measure the relative prices of exports to imports; and trade openness ratios, typically expressed as the sum of exports and imports relative to GDP (Yusuf & Magaji, 2023; Odungweru&Ewubare, 2020).

2.1 Theoretical Framework

The Keynesian public-expenditure tradition, grounded in the ideas of John Maynard Keynes and later elaborated in modern macroeconomic policy literature, posits that government spending is a powerful instrument for stabilizing aggregate demand and stimulating output, particularly during periods when private sector demand is insufficient. At the heart of Keynes's argument is the view that fluctuations in aggregate demand drive short-run variations in output and employment; consequently, countercyclical fiscal actionssuch as increases in public spending or reductions in taxescan revive demand and support economic recovery. Subsequent scholarship and policy analysis extended this reasoning by highlighting the distinctive effectiveness of public capital expenditure, especially investments in roads, power, water systems and other forms of social overhead capital. Such spending not only generates immediate demand through wages, procurement and construction activity, but also enhances long-term productive capacity by improving the infrastructure base on which private investment and economic activity depend (Babalola, 2015; Ojo et al., 2023).

The Keynesian logic is often invoked to justify public investment as a direct stimulus for contractors, material suppliers and labour markets: a well-timed capital programme creates contracts, increases capacity utilization and generates employment in the short run while improving infrastructure that lowers private production costs in the medium term (Edame, Udude, & Ugwu, 2014; Ojo et al., 2023). Empirical studies in Nigeria that find positive

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

associations between public capital spending and sectoral output typically interpret results through this Keynesian lens (Edame et al., 2014; Osinowo, 2015).

From a Keynesian perspective, foreign trade outcomes are strongly influenced by the level of aggregate demand, which fiscal policy directly shapes. Keynesian theory argues that when the government increases spending or reduces taxes, aggregate demand rises, leading to higher domestic income and output. Because part of this additional income is spent on imported goods, expansionary fiscal policy tends to increase imports, potentially widening the trade deficit,an effect widely known as the absorption approach to the balance of payments (Onuchuku&Obayori, 2018). This mechanism is consistent with the Keynesian view that domestic expenditure determines the demand for both domestic and foreign goods; thus, fiscal expansion raises total absorption, including import demand.

2.2 Empirical Literature

Nigerian evidence and related studiesare extensive but mixed.Jones et al. (2025) examined the impact of monetary policy on Nigeria's export sector using monthly data from 2014 to 2023 and an Error Correction Model (ECM). Their findings show that historical export performance is the strongest predictor of current export levels, indicating high persistence in export behaviour. The study also reports that the real effective exchange rate exerts a positive influence on export performance, suggesting that exchange-rate movements remain a key determinant of external competitiveness. Using a combination of cointegration and error-correction techniques, Nwagu et al. (2022) investigated the nexus between fiscal policy, monetary policy, and Nigeria's trade balance. Their results reveal a long-run relationship among fiscal variables, monetary indicators, and trade outcomes. Specifically, the study finds that fiscal expansion, particularly through government expenditure, tends to worsen the trade balance, consistent with the Keynesian absorption approach.

Odungweru and Ewubare (2020) assessed the effect of monetary policy on Nigeria's international trade between 1980 and 2017 using an ECM framework. Their findings indicate that the exchange rate has a significant positive effect on foreign trade in the long run, while the minimum rediscount rate exerts a significant negative effect. Money supply was also found to influence trade flows, though with mixed signs across the short and long run. The authors conclude that monetary policy remains a critical determinant of Nigeria's trade performance, particularly through its influence on exchange-rate stability and credit conditions.

In a related ECM-based study, Ashamu (2020) investigated the impact of monetary policy on foreign trade from 1981 to 2017. The results show that the exchange rate and money supply positively affect foreign trade, while the interest rate exerts a negative influence. The study

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

suggests that Nigeria's trade sector responds favourably to expansionary monetary conditions, provided that exchange-rate volatility is contained. The findings reinforce the view that macroeconomic stability is essential for improving trade outcomes.Eze and Eze (2020) conducted a comparative analysis of fiscal and monetary policy effectiveness on Nigeria's net exports using ARDL and Granger causality tests. Their results show that money supply has a positive but insignificant effect on net exports, while interest rate and exchange rate exert negative but insignificant effects. Fiscal variables also showed weak explanatory power. The study concludes that neither fiscal nor monetary policy has been sufficiently effective in driving Nigeria's external sector, largely due to structural rigidities and policy inconsistencies.

Focusing specifically on fiscal policy, Onuchuku and Obayori (2018) examined the impact of government capital expenditure, corporate tax, and external debt on Nigeria's balance of payments using VECM and cointegration techniques. Their findings show that government capital expenditure has a positive and significant effect on the balance of payments, while corporate tax exerts a negative effect. External debt was found to have a positive but mixed impact depending on the time horizon. The study concludes that fiscal policy, particularly capital spending, plays a crucial role in shaping Nigeria's external sector performance.Onwe and Okoro (2015) investigated the impact of fiscal policy on non-oil export trade in Nigeria. Their results indicate that fiscal policy variables, particularly taxation and government expenditure, significantly influence non-oil exports, though the direction of impact varies across models. The study highlights the sensitivity of non-oil exports to fiscal incentives and the need for targeted tax reforms to stimulate export diversification.

3.0 METHODOLOGY

This study attempts to ascertain the link between fiscal policy and foreign trade performance in Nigeria, using annual time series data spanning 35 years from 1990 to 2024, obtained from the Central Bank of Nigeria (CBN) statistical bulletins. To analyze the data, the ADF unit root, as well as the Auto Regressive Distributed Lag (ARDL) model. The model is specified as:

$$TRDINT = f\ (GCE, GRE, FDF) \quad (1)$$

Transforming the structural econometric model to regression model,

$$TRDINT = \alpha_0 + \alpha_1 GCE + \alpha_2 GRE + \alpha_3 FDF + \mu \quad (2)$$

Where TRDINT = Trade Intensity (Openness)
GCE = Government Capital Expenditure
GRE = Government Recurrent Expenditure

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

FDF = Fiscal Deficit
α_0 = Constant
$\alpha_1 - \alpha_3$=Coefficients of independent variables
μ = Error Term
By apriori, $\alpha_1, \alpha_2 > 0 > \alpha_2$

4.0 RESULTS AND DISCUSSION

Table 1: Descriptive Statistics

	TRDINT	GCE	GRE	FDF
Mean	33.64187	31.23721	63.64548	28.27735
Median	34.30580	27.10451	67.32434	24.56492
Maximum	55.02120	63.44077	80.28548	73.39992
Minimum	17.85611	11.15642	36.56333	-11.83274
Std. Dev.	8.852996	14.21038	11.14246	20.89402
Skewness	0.274989	0.923930	-1.088257	0.117477
Kurtosis	2.627520	2.945421	3.609790	2.467917
Jarque-Bera	0.643443	4.983946	7.450707	0.493376
Probability	0.724900	0.082747	0.024105	0.781384
Observations	35	35	35	35

Source: Researcher's Computation with EViews

On average, GRE records the highest level (mean ≈ 63.65) while FDF posts the lowest mean (≈ 28.28), with TRDINT and GCE clustered in the low-to-mid 30s. FDF is the most variable (std. dev. ≈ 20.89) and displays the widest relative dispersion; whereas GRE is the most stable (std. dev. ≈ 11.14). GRE is noticeably left-skewed (skewness ≈ −1.09) with leptokurtic tails (kurtosis ≈ 3.61), while GCE is moderately right-skewed, and TRDINT and FDF are close to symmetric. Jarque–Bera tests indicate that GRE departs significantly from normality (p ≈ 0.024), GCE is borderline non-normal (p ≈ 0.083), and TRDINT and FDF do not reject normality at conventional levels.

Table 2: Augmented Dickey-Fuller (ADF) Unit Root Test

Variables		**t-statistic**	**Critical value (0.05)**	**Prob.**	**Order of Integration**
FDF	Level	-2.028365	-2.951125	0.2739	*I*(1)
	1st Difference	-5.334905	-2.954021	0.0001	

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

GCE	Level	-1.669819	-2.951125	0.4370	*I*(1)
	1st Difference	-5.819872	-2.954021	0.0000	
GRE	Level	-2.210656	-2.951125	0.2063	*I*(1)
	1st Difference	-6.464232	-2.954021	0.0000	
TRDINT	Level	-3.144538	-2.951125	0.0326	*I*(0)

Source: Researcher's Computation with EViews

The results in Table 1 indicate that all variables are stationary and integrated at their first differences, *I*(1), except for TRDINT, which is integrated at the level, *I*(0).

Table 3: ARDL Bounds (Cointegration)/Long-run Test

Variable	Coefficient	Std. Error	t-Statistic	Prob.
GCE	0.493315	0.237660	2.075716	0.0472
GRE	0.290715	0.299986	0.969096	0.3408
FDF	-0.132806	0.072509	-1.831576	0.0777

EC = TRDINT - (0.4933*GCE + 0.2907*GRE -0.1328*FDF)

F-Bounds TestNull Hypothesis: No levels relationship

Test Statistic	Value	Signif.	I(0)	I(1)
			Asymptotic: n=1000	
F-statistic	4.375868	10%	2.72	3.77
K	3	5%	3.23	4.35
Actual Sample Size	34	1%	4.29	5.61

Source: Researcher's Computation with EViews

The F-statistic of 4.376 in Table 3 is greater than the critical values at the *I*(1) and *I*(0) bounds, rejecting the null hypothesis of no cointegration. Thus, a dynamic long-run relationship exists between the variables.

Table 4: ARDL Error Correction Test

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	3.226800	1.184699	2.723729	0.0110
D(FDF)	-0.277997	0.074827	-3.715188	0.0009
CointEq(-1)*	-0.861463	0.195692	-4.402141	0.0001

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

R-squared	0.599154	Mean dependent var	0.537754
Adjusted R-squared	0.573293	S.D. dependent var	9.150664
S.E. of regression	5.977471	Akaike info criterion	6.497969
Sum squared resid	1107.635	Schwarz criterion	6.632648
Log likelihood	-107.4655	Hannan-Quinn criter.	6.543899
F-statistic	23.16822	Durbin-Watson stat	1.864478
Prob(F-statistic)	0.000001		

Source: Researcher's Computation with EViews

The ARDL error-correction results in Table 4 indicate a negative and highly significant error-correction term (−0.8615, $t = -4.402$, $p = 0.0001$), which confirms cointegration and shows rapid adjustment: about 86% of any disequilibrium is corrected within one period. However, only the D(FDF) coefficient is significant,though negative (−0.2780, $t = -3.715$, $p = 0.0009$), implying that an increase in FDF is associated with an immediate reduction in the dependent variable in the short run.

Discussion of findings

In the long run GCE enters positively and significantly (coefficient ≈ 0.493, $p = 0.047$), indicating that higher public capital spending is associated with higher trade intensity or improved external performance; this conforms with the a priori expectation that investment in roads, ports, power and other trade-enabling infrastructure raises productive capacity and lowers trade costs (Onuchuku&Obayori, 2018; Ojo et al., 2023). Sustained increases in GCE translate into materially higher trade outcomes. This result aligns with Onuchuku and Obayori's finding that capital spending improves the balance of payments and with policy literature stressing composition over the size of spending.

Similarly, GRE has a positive but statistically insignificant long-run coefficient (≈ 0.291, $p \approx 0.341$), so the evidence does not support a robust long-run effect of recurrent spending on trade intensity in this sample. A priori, the sign is ambiguous: recurrent outlays can stimulate demand (raising imports) or support services that indirectly aid trade, but they are less likely than capital spending to raise tradable capacity (Onwe & Okoro, 2015; Eze & Eze, 2020). The insignificance here suggests recurrent spending in Nigeria has not consistently translated into improved external performance, which is consistent with studies that find recurrent-heavy budgets often fail to enhance competitiveness and may even widen import demand when poorly targeted.

FDF shows a negative long-run coefficient (≈ −0.133, $p \approx 0.078$), borderline significant, and a clearly negative and highly significant short-run effect on the dependent variable (ΔFDF

ISSN: 3049-3552

Volume 4 Issue 4, July-August 2026, pp 117-128

coefficient ≈ −0.278, p = 0.0009). Both estimates point in the same direction: increases in fiscal deficits or adverse financing conditions are associated with weaker trade intensity. This conforms with Keynesian absorption logic that fiscal expansions financed in ways that raise domestic absorption or appreciate the real exchange rate tend to worsen external outcomes (Nwagu et al., 2022; Onuchuku&Obayori, 2018). The short-run result implies that deficit shocks quickly translate into lower trade performance (probably via import surges, exchange-rate pressures, or crowding-out of private tradable investment), while the long-run negative coefficient suggests persistent deficits can erode competitiveness over time. These findings echo empirical work showing that the mode and sustainability of deficit financing matter for trade outcomes (DMO, 2018; Festus & Saibu, 2023).

5.0 CONCLUSION

The study examined the nexus between fiscal policy and foreign trade prospects of Nigeria, estimating the influences of public expenditure (capital and recurrent) and fiscal deficits on trade intensity. The study showed a stable long-run relationship between trade intensity and the fiscal variables, with rapid correction of disequilibria. It concludes that composition and financing of fiscal policy matter more than headline size: public capital spending supports trade, while deficits and poorly targeted recurrent spending undermine it. To this end, it recommends the following:

1. Prioritize and protect budgetary allocations to high-impact infrastructure projects (roads, ports, power, water) with clear project selection criteria and cost-benefit appraisal andstrengthen public investment management (project appraisal, procurement, implementation monitoring) to ensure timely completion andmaximize trade-related returns.
2. Reorient recurrent spending toward trade-supporting services (customs modernization, export promotion, maintenance of infrastructure) and efficiency gains (digitalization, public sector reform), as well as avoid recurrent spending growth that is not matched by productivity improvements in tradable sectors.
3. Tighten fiscal discipline by improving revenue mobilization (broadening tax bases, strengthening compliance) and prioritizing deficit reduction strategies that protect capital spending whilefavouring market-based, long-term domestic borrowing and concessional external finance for investment over monetization.
4. Develop a medium-term fiscal framework that explicitly links deficit paths to trade and competitiveness objectives and conducts stress tests for exchange-rate and external-financing risks.

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