

Innovations

Responsiveness of the Stability of the Financial System to Fiscal Shocks: A Sub-Saharan Africa (SSA) Perspective

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Abstract: *The study evaluated the impact of fiscal shocks on financial system stability in Sub-Saharan Africa for the coverage period, 1973 to 2023 and the cross section represents 48 countries in Sub-Saharan Africa. The independent variables were Revenue Shock, Public Expenditure Shock, Public Debt Shock, Growth Shocks, Interest Rate and Exchange Rate Shocks, which were used to measure fiscal shocks while the dependent variable is financial system stability measured by Z-score. Using dynamic panel least squares, the study found that Fiscal shocks arising from public expenditure, growth and*

revenue adversely affected financial system stability while those arising from debt and interest rate positively and significantly affected the stability of the financial system in SSA countries within the investigated period. This study exposes the fact that the stability of the financial is not only a monetary policy issue rather fiscal policy also can help stabilize or add to the destabilization of the SSA countries financial system. This factor is amplified by the fragility of the SSA financial system and the fiscal dominance in the management of the economy of the region which makes policy retooling imperative for averting system failures and destabilisation.

Keyword: *Fiscal Shocks, Volatility Series, SSA Countries, Financial system stability.*

1. Introduction

Financial stability remains an ongoing concern for the financial systems in Sub-Saharan Africa. Achieving and maintaining financial stability extend beyond the absence of financial crises; it involves creating an environment where financial institutions operate efficiently, markets function smoothly, and economic activities flourish (Beck, Demirgüç-Kunt, & Levine, 2007). However, the trajectory of financial stability in the region has been characterized by fluctuations, and fiscal shocks have emerged as critical destabilizing factors.

The adoption structural adjustment programs through the directive of international financial institutions around the late 20th century further underscored the complexities of the region's economic landscape (World Bank, 2000). While these programs aimed to address economic imbalances, they often led to social hardships and strained financial systems. Consequently, Sub-Saharan Africa's financial environment became intricately entwined with historical legacies, shaping its resilience to external shocks, including fiscal shocks.

Fiscal shocks, defined as sudden and significant changes in government spending or revenue, have emerged as recurring challenges for Sub-Saharan Africa (Celasun, Debrun, & Ostry, 2006). These shocks can result from diverse factors, including shifts in government policies, global economic conditions, or unforeseen events like natural disasters or health crises. The impact of fiscal shocks extends beyond immediate economic consequences, influencing the solvency of banks, investor confidence, and the overall stability of financial markets.

The vulnerability of Sub-Saharan African financial systems to fiscal shocks is intricately linked with historical and structural challenges. The reliance on commodity exports, volatility in global markets, and limited economic diversification have collectively heightened the region's susceptibility to external shocks (Ncube & Lufumpa, 2011). Understanding the historical context and the dynamics of fiscal

shocks is fundamental to comprehending the intricate relationship between Sub-Saharan Africa's financial systems and external economic forces.

The core problem lies in unraveling the intricate ways in which fiscal shocks reverberate through the financial architecture of Sub-Saharan Africa (Kpodar, 2005). Acknowledging the existence of these shocks is only the beginning; understanding their multifaceted impacts is essential. These impacts extend beyond economic indicators to affect the solvency of banking institutions, investor confidence, and the overall functioning of financial markets. As highlighted by Gupta, Baldacci, & Mati (2004), the challenge is not only in preventing the occurrence of fiscal shocks but also in fortifying the financial systems to absorb and recover from these shocks effectively.

The gravity of the problem becomes evident when considering the potential consequences of financial instability. A lack of stability can impede economic growth, hinder investment, and exacerbate poverty (Honohan & Laeven, 2005). Financial instability can create a vicious cycle, where economic downturns lead to increased fiscal pressures, contributing to further instability. Recognizing the intricate relationship between fiscal shocks and financial stability is essential for developing effective strategies to mitigate these challenges.

Finally, with the increasing degree of fiscal indiscipline, policy inconsistency, and uncertainties in Sub-Saharan African countries, there are bound to be shocks and responses from fiscal policy variables. How these shocks are transmitted to the financial system as well as the concomitant effect of such transmission should be of investigative interest

It is against this backdrop that this work is set to look at the impact of the volatility series of fiscal variables (fiscal shocks) on the stability of the financial system in SSA countries.

The study's significance is underscored by the persistent challenges faced by Sub-Saharan African countries in achieving sustained economic growth and financial system stability. Therefore, it is particularly relevant in the current global context, where the world has been grappling with unprecedented challenges ever since the outbreak of such COVID-19 pandemic and its economic setback.

The dynamics of fiscal shocks are crucial for developing adaptive strategies that can fortify financial systems against unexpected disruptions. The study aims to provide actionable insights for policymakers navigating the complex terrain of economic governance. Policymakers in Sub-Saharan Africa, armed with a nuanced understanding of the impact of fiscal shocks, can formulate targeted interventions to enhance financial resilience and stability.

International financial and supranational organizations play a crucial role in supporting economic development in Sub-Saharan Africa. The findings of this study

will offer valuable insights for these organizations to tailor their assistance programs, ensuring they address the specific challenges posed by fiscal shocks. Financial institutions operating in Sub-Saharan Africa, including central banks and commercial banks, will benefit from a deeper understanding of the dynamics between fiscal shocks and financial stability. This study provides insights that can inform risk management strategies, capital planning, and overall decision-making processes within these institutions.

Findings arising from this study will also be useful to researchers and scholars, as it will form a basis for further research aside from contributing to the pool of knowledge on the nexus between determining factors of monetary and fiscal policy shocks on the economic stability of all SSA countries and beyond, therefore contribute to the academic body of knowledge.

In evaluating the interaction between fiscal shocks and financial system stability, which is the main thrust of this study, the conceptual interconnectedness follows the form shown in Fig. 2.1 below:

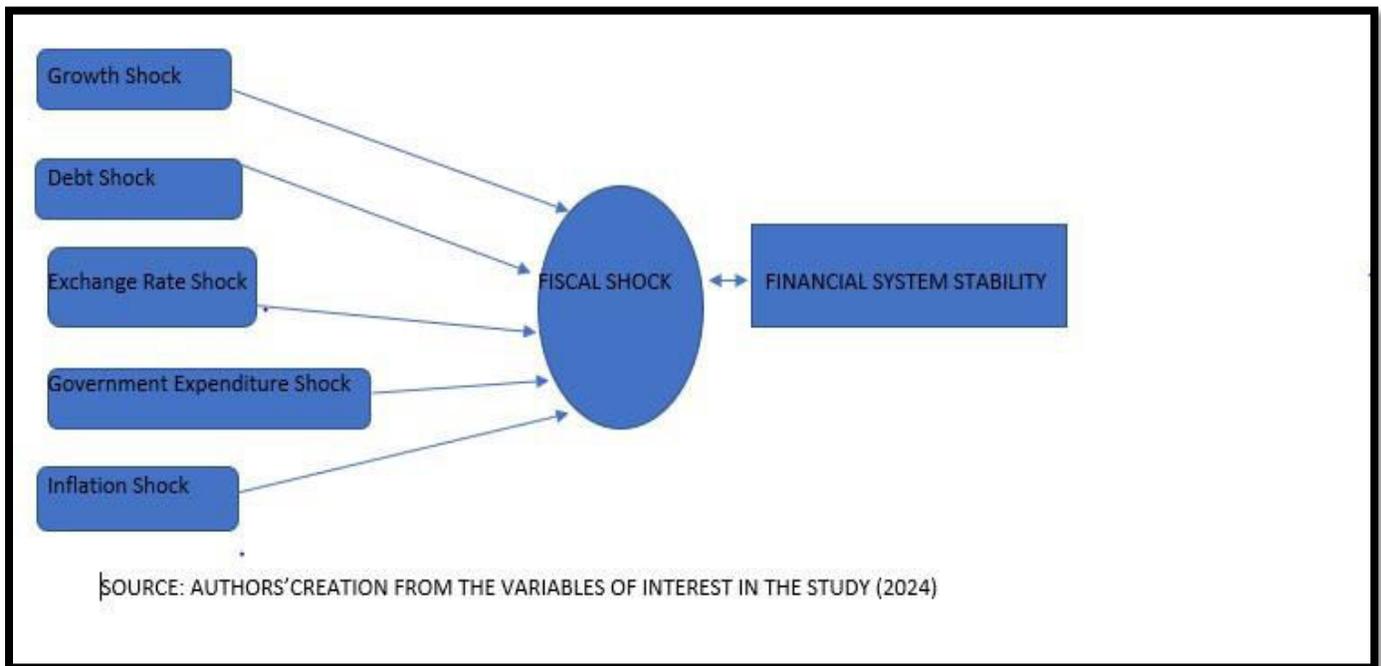


Fig. 2.1 – Fiscal Shocks and Financial Stability Nexus

We evaluate within the context of SSA countries the variables of interest in this study. Firstly, we observed that financial system stability indicator has maintained a volatile movement probably due to the influences of endogenous and exogenous factors within the region. This is captured from the Fig. 2.2 below:

FIG. 2.2 - % CHANGE IN SSA COUNTRIES Z-SCORE

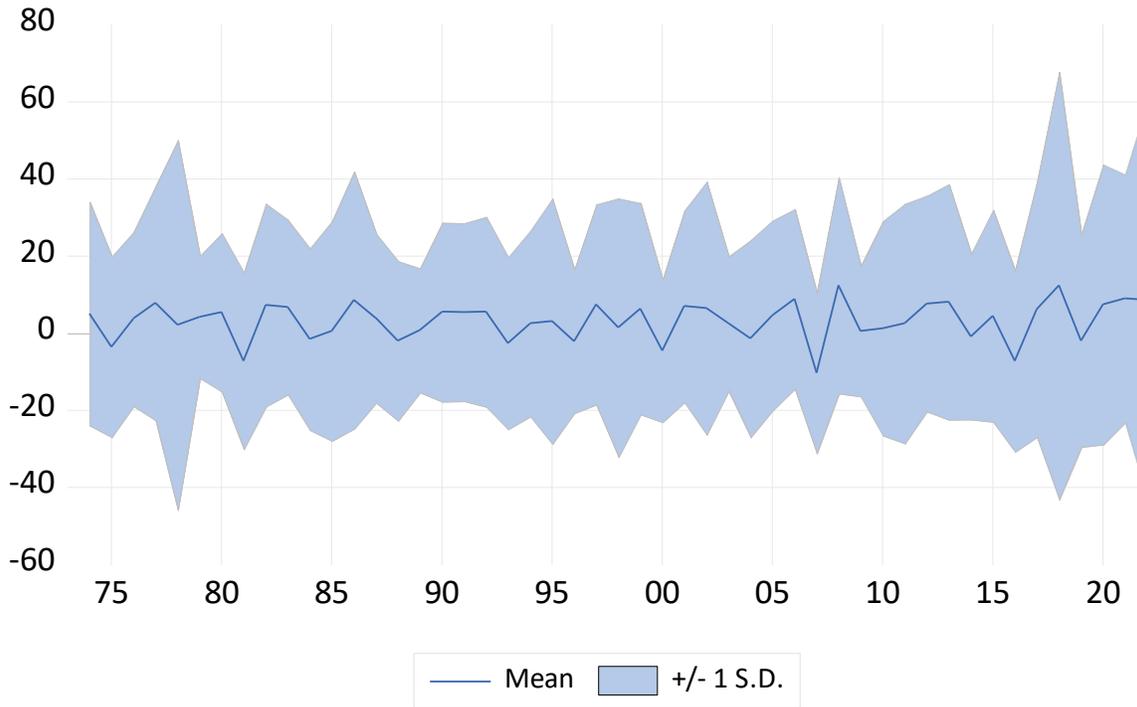


Fig. 2.2 Movement in Financial System Stability Indicator

The mean and standardized variance plot of Z-score shows instability in the system and prompts an investigation into the causal factors for this movements. The biggest dip is observed between 2007 and 2010 which were the periods of the global financial crises.

Contextual movements in the other explanatory variables are shown in graphs below:

FIG. 2.3 - GROWTH SHOCK FOR SSA 1980 - 2023

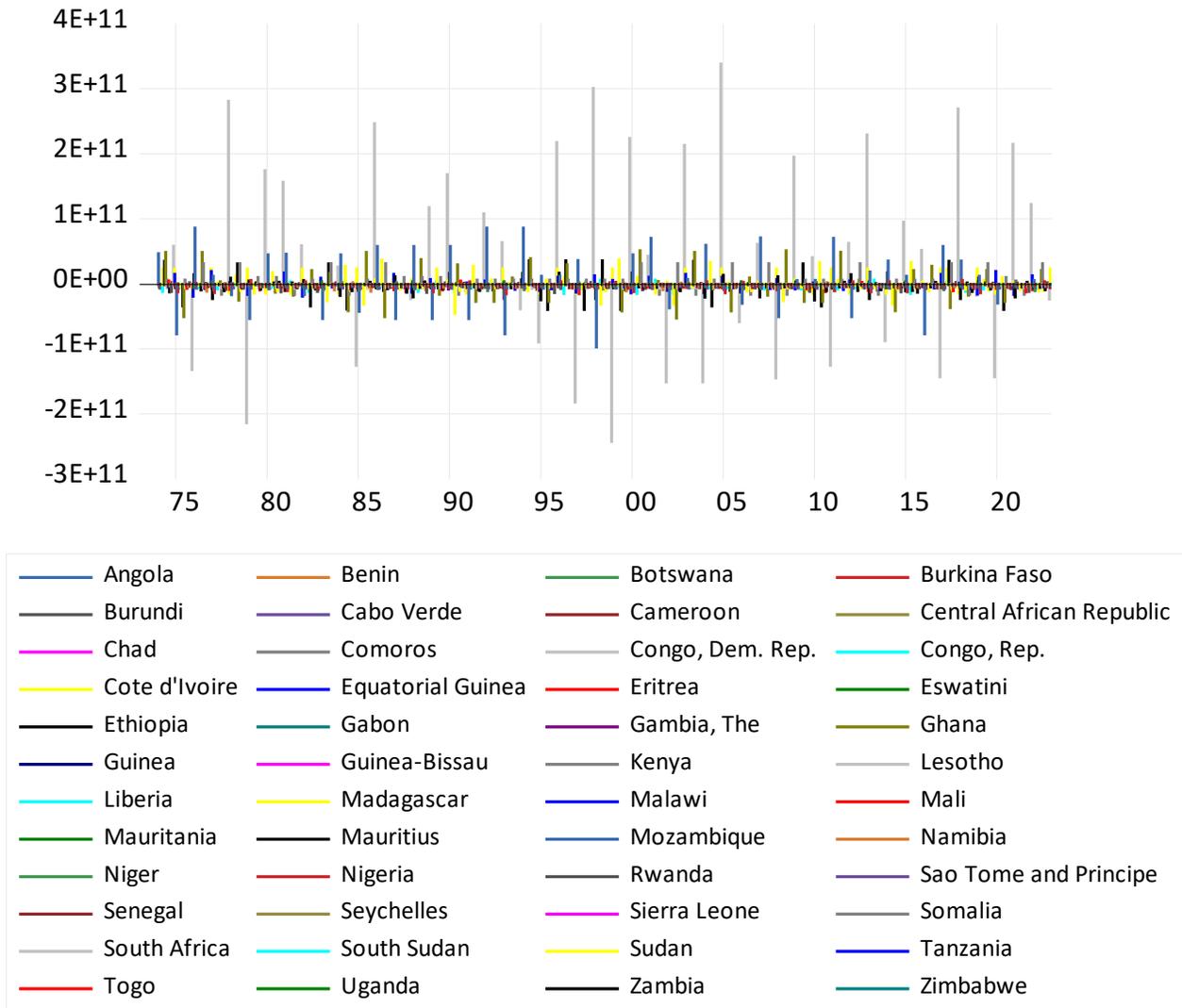


Fig. 2.3 – Growth Shock for SSA Countries, 1980 - 2023

Fig. 2.3 shows consistent growth instability in the region, there are spikes in growth within the investigated period suggesting that the financial system can be predisposed to shocks emanating from growth volatility.

Movement in other explanatory factors to financial system stability within the context of this study is presented in Fig. 2.4 to 2.8 respectively.

The volatility in interest rate and exchange rate is shown in fig 2.4 and 2.5 respectively indicating that shocks from these two variables can be contributory to fiscal shocks which can be an influencer of financial system stability in SSA.

FIG 2.4 - REAL INTEREST RATE FOR SSA 1980 - 2023

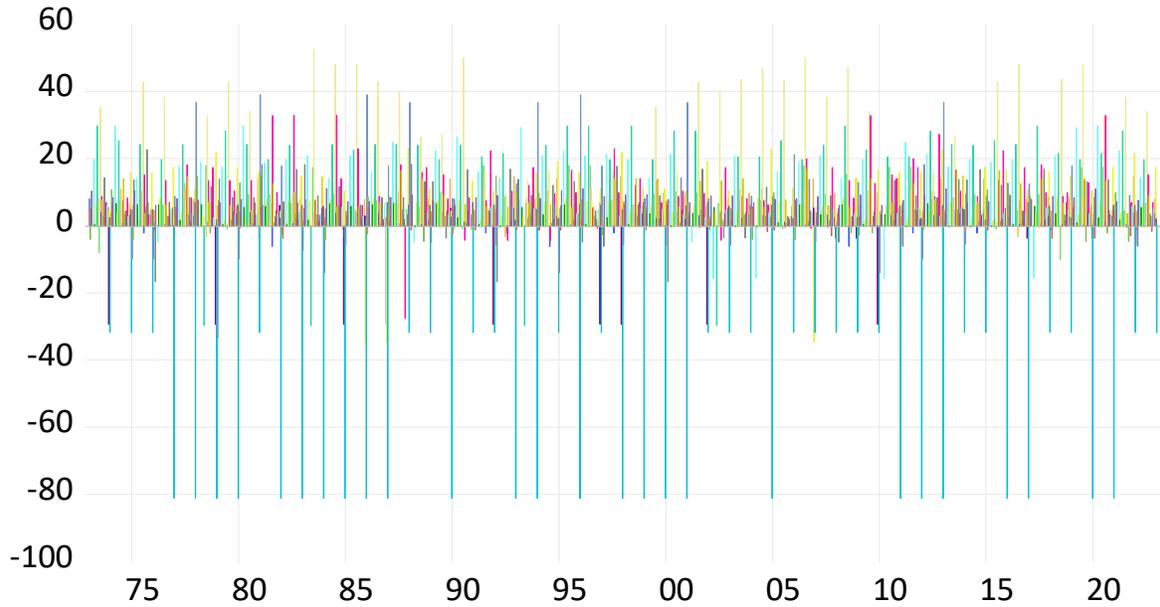


FIG 2.5 - EXCHANGE RATE OSCILLATION IN SSA

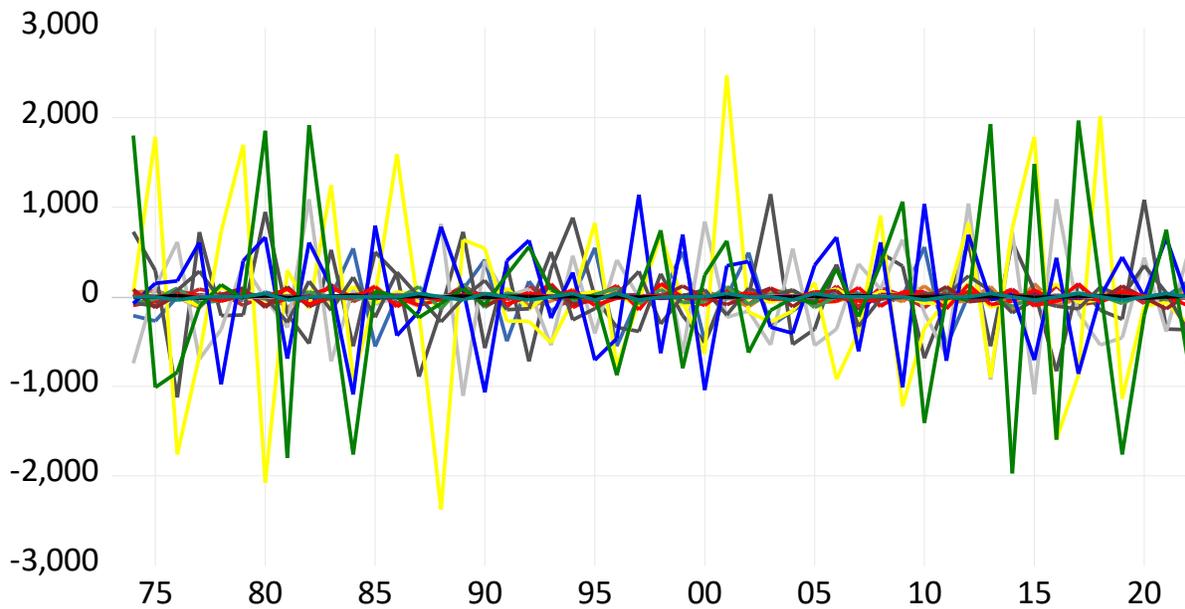


Fig. 2.6 – 2.8 respectively presents movement in revenue, expenditure, and debts. According to Olaoye, Omokanmi, Tabash, Olofinlade, & Ojelade (2024) are significant contributors to fiscal shocks.

FIG 2.6 - A PLOT OF SSA RGOVERNMENT REVENUE GROWTH SHOCK 1980 TO 2023

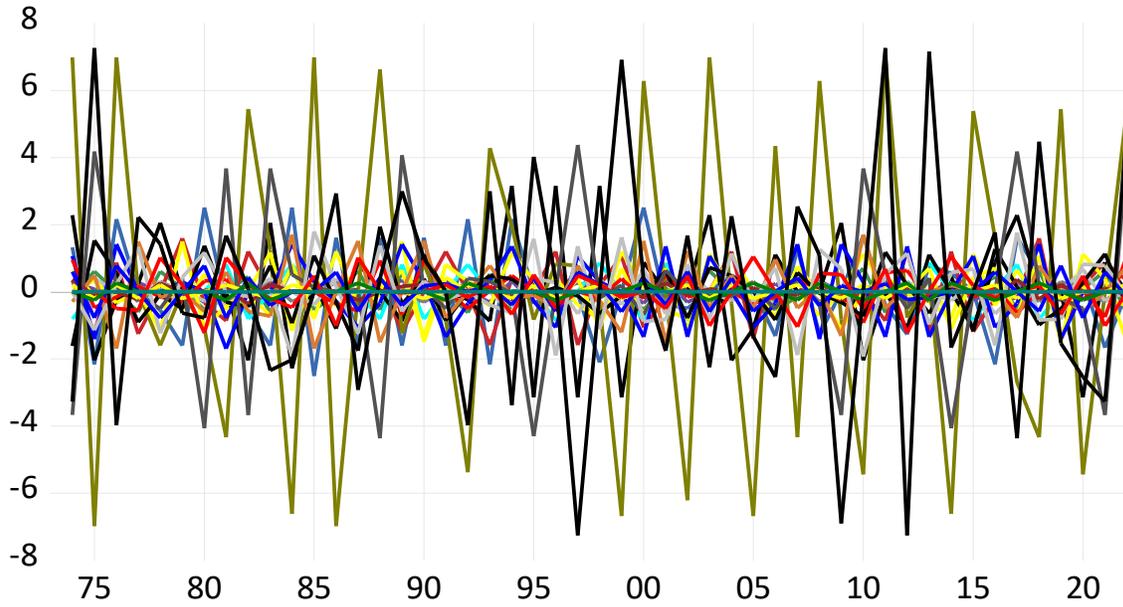


FIG. 2.7 - A LINE PLOT OF OSCILLATION IN GOVERNMENT REVENUE IN SSA 1980 TO 2023

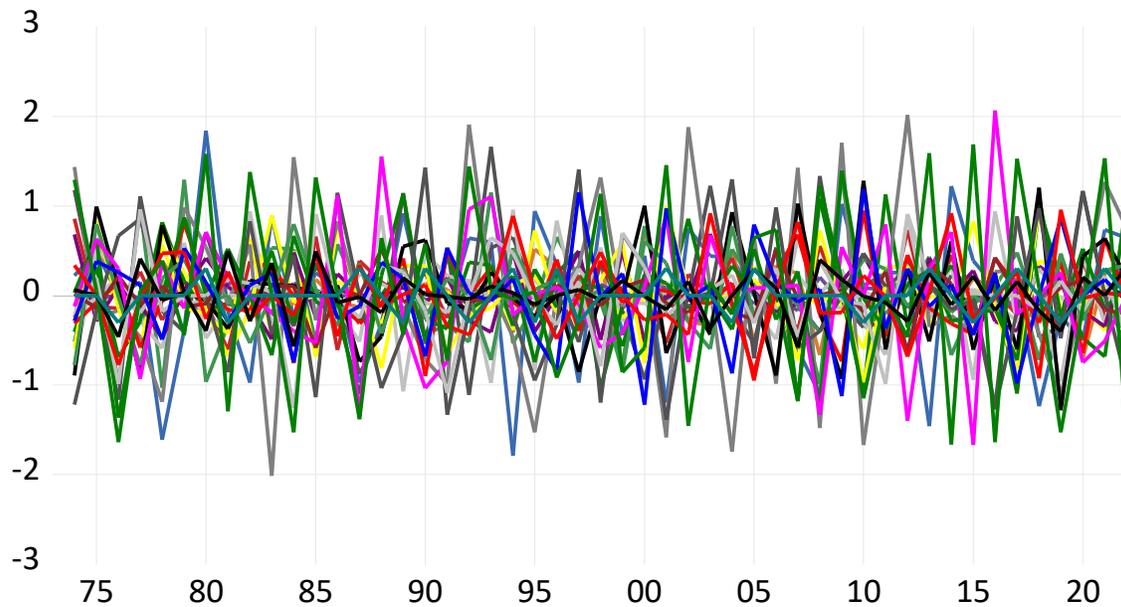
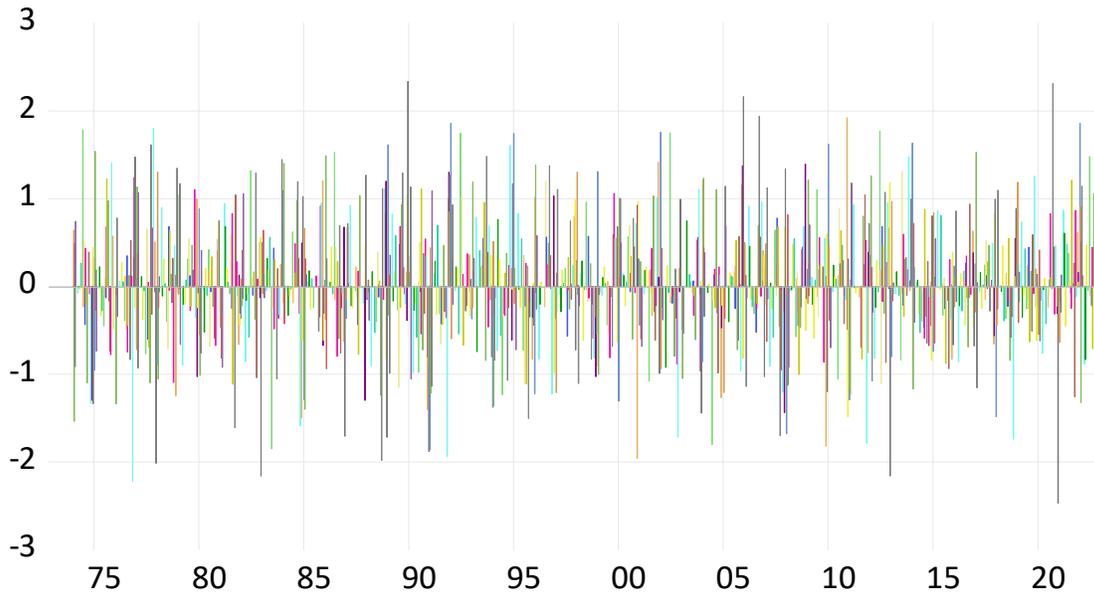


FIG. 2.8 - BAR PLOT OF THE LOG DIFFERENCED FORM OF PUBLIC DEBT IN SSA 1980 TO 2023



Putting all the variables of interest in context, it can be said that the interconnectedness of the variables of interest in the SSA economic space, is of investigative interest.

This study is therefore organised as follows: section one introduces the study, a brief review of literature is presented in section two, the methodology of the study is presented in section three and the empirical data analysis is in section four while section five concludes.

2. Literature review

Some of the study that have looked at fiscal policy and how it affects financial system stability in SSA countries include Olaoye et al, (2024) who used generalized method of moments (system GMM) to investigate fiscal policy and inflation rate in (SSA) countries over 2003–2020. The study found that there is interconnectedness between fiscal shocks and financial system stability. This view is shared by Damane, Moeti and Ho (2024) for SSA countries and Majeed et al. (2024) who made a similar finding for Australia with the overall, the results suggesting that monetary policy and economic conditions are important stabilization policies for the financial system.

Approaching from the perspective of risk-taking and instabilities, Gondwe (2023) investigated regulations as a mitigating factor against Bank risk (instability) in SSA from 2009 to 2019. The overall results show that regulations are effective in reducing solvency risk.

From a fiscal shock perspective, Attahir (2016) empirically investigated the effect of fiscal policy shocks on output and unemployment in Nigeria and found from the SVAR model that shock from both public expenditure and revenue have a positive long-term effect on output. This is supported by findings from Siwińska-gorzela(2023) and Lawal and Kayit (2023) who concluded that fiscal volatility impact on macroeconomic performance in Nigeria.

Studies on fiscal policy and financial stability nexus have had varied conclusions. Borio, Farag and Zampolli (2023) and Francisco, Antonio, and Garima (2023) both agreed that addressing the nexus between fiscal policy and financial stability is imperative for macroeconomic stability. This position is supported by Woldu (2023) in a study of 40 sub-Saharan countries arriving at a conclusion that fiscal consolidation not only affect stability, but it also reduces real GDP and private demand. Ricky-okine et al. (2023) found that fiscal policies implementation and directives in SSA drives financial sector development; thus, leading to economic growth. Merrino (2021) concludes on the crowding out effect of fiscal expansion on private economic activity including the financial system. Ilesanmi (2020) holds that a sound and stable financial system is threatened by fiscal shocks as was shown by the global financial crisis (GFC), in a study that covered the period 2000 to 2017. Dumičić (2019) not only show the effect of shocks on the stability of the financial system but also held that public debt, tax, government revenue and other fiscal exposures serve as transmission mechanisms for shocks to the financial system. This transmission exposure of the financial system to fiscal policy and the attendant shocks is also supported by Makrelov et al (2018) and Ibrahim and Alagidede (2017)

In addressing the impact of fiscal on some advanced financial systems, Zhang and Barnett, (2014) showed how China weathered the global financial crisis through by observing that augmented fiscal deficit and debt had a positive effect on the financial system. This supports the dynamic interaction between monetary policy and fiscal policy as observed by Dianta (2013) in Indonesia for the period of 1999 to 2010. Other supportive studies include Gali and Perotti (2002), Marneffe (2011), Ballabriga and Martinez (2003) for the European Union; Viren (2002) for OECD countries; and Tapsoba (2012) for 74 developing countries.

Following a review of conceptual, theoretical, and empirical literature on the interaction between financial system stability and fiscal shocks, the study identified some gaps which are theoretical, jurisdictional, and temporal which are presented thus:

- Most of the investigated studies have approached the drivers of financial stability from a micro-theoretical perspective. This means they have given much attention to industry specific drivers of financial stability. This study differs markedly from those studies by making this an investigation into

financial stability from a macro-theoretical perspective. The macroeconomic factors viewed from the prism of fiscal policy and the attendant shocks are to be evaluated as impacting variables with financial stability as a response variable.

- Jurisdictionally, this study investigates SSA countries. There is scarcity of studies that have focused on the impact of the fiscal space on the stability of the financial system and scarcer are the ones that have evaluated fiscal shocks against financial system stability. Policy uncertainties, social, economic and political instabilities in SSA countries make them predisposed to shocks. With the prevalence of shocks from the fiscal space comes the need to investigate the transmission effect of such shocks to the financial system. This is a jurisdiction or spatial gap that this study fills.
- From the multidimensionality of the reviewed literature, it is evident that though they may be consensus as per the overall adverse impact of shocks there is no consensus on the impact of the individual causes of fiscal shock on financial system stability. It is important to fill the gap in literature on how shocks from growth, price level, exchange rate, unemployment and other fiscal policy factors respectively affect financial system stability. This is an empirical gap that this study intends to fill.

3. Methodology

Data and Model

The dataset for this study follows the panel form with its cross sectional and time dimension. It investigates the responsiveness of the stability of the financial system to fiscal shocks focusing on 48 SSA countries in with the world bank classification. The data are drawn from the world development indicators, a repository of the world bank and global financial development database (GFDD) by the international monetary fund's Financial system stability is proxied by the Bank Z-score given the dominance of the banking sector in the financial space of SSA countries. The explanatory variables which are shocks from key fiscal policy indicators include revenue shocks, growth shock, exchange rate shock, debt shock, public expenditure shock with interest rate shock acting as the moderating variable.

The shocks series were derived as the volatility series of the contemporaneous values of the fiscal variables. The estimation is of the form of a GARCH (1,1) model shown below:

$$y_t = X_t' \theta + \varepsilon_t \quad (Eq. 1)$$

$$\sigma_{t_t}^2 = \omega + \alpha \varepsilon_{t-1}^2 + \beta \sigma_{t-1}^2 \quad (Eq. 2)$$

While Equation 1 stands for the mean equation and 2models conditional variance and the volatility series of each of the variables represents their respective shocks of each of them respectively.

The functional relationship that this study investigates is presented thus:

$$FSS = f(FS) \tag{3}$$

Where FSS = Financial System Stability and FS = fiscal shocks with f= functional notation. A disaggregation of fiscal shocks presents the relationship shown in equation 4.

$$FSS = f(RS, PES, PDS, GS, INTRS, EXRS) \tag{4}$$

Where:

FSS = Financial System Stability, RS = Revenue Shocks, PES = Public Expenditure Shocks,

PDS= Public Debt Shocks, GS = Growth Shocks, INTRS = Interest Rate Shocks, EXRS =Exchange Rate Shocks and f= functional notation.

The general model for this study is specified in an estimable panel framework as follows:

$$FSS_{it} = \delta_o + \delta_1 RS_{it} + \delta_2 PES_{it} + \delta_3 PDS_{it} + \delta_4 GS_{it} + \delta_5 INTRS_{it} + \delta_6 EXRS_{it} + \mu_{it} \tag{5}$$

All the variables are as defined in equation 4while δ_o = constant or the intercept, $\delta_1 - \delta_6$ =coefficients of the parameters or explanatory variables, μ_{it} = the residual or error term.

Applying a panel estimation technique such as the dynamic panel estimation framework will make the model to be rewritten as follows:

$$\begin{aligned} FSS_{it} = & \delta_o + \sum_{t=1}^k \delta_1 FSS_{it-1} + \sum_{t=1}^k \delta_2 RS_{it-1} + \sum_{t=1}^k \delta_3 PES_{it-1} + \sum_{t=1}^k \delta_4 PDS_{it-1} \\ & + \sum_{t=1}^k \delta_5 GS_{it-1} + \sum_{t=1}^k \delta_6 INTRS_{it-1} + \sum_{t=1}^k \delta_7 EXRS_{it-1} + \varphi_1 FSS_{it-1} \\ & + \varphi_2 RS_{it-1} + \varphi_3 PES_{it-1} + \varphi_4 PDS_{it-1} + \varphi_5 GS_{it-1} + \varphi_6 INTRS_{it-1} \\ & + \varphi_7 EXRS_{it-1} + \mu_{it} \tag{6} \end{aligned}$$

δ_o = constant or the intercept

$\delta_1 - \delta_7$ = coefficients of short-run parameters or explanatory variables

$\varphi_1 - \varphi_7$ = coefficients of the long-run parameters or explanatory variables

μ_{it} = the residual or error term.

All the variables are as defined above with the only new introduction being INF – Inflation which serves as the moderating variable.

The analytical framework of the study follows three steps. First are the pre-estimation tests, which tests that will prove the goodness of the dataset for the main econometric/statistical estimation of this study. These will include Panel Descriptive Statistics, Panel Correlational Analyses and Panel Unit Root tests

Secondly, the main estimation method is a dynamic panel least squares which has superiority of the static panel estimators. This is made necessary by the fact that the series are to be predictive instead a contemporaneous measurement of responsiveness.

Lastly, an array of diagnostic tests are deployed to affirm the reliability and validity of the obtained estimates from step 2. Also, the inferences and conclusions made on this study follow the validated estimates.

4. Results

First, the basic panel descriptive statistics for this study is shown in table 1. This is a necessary first step for the determination of the distributional characteristics of the panel series.

Table 1: Summary of Panel Descriptive Statistics.

	Mean	Median	Maximum	Minimum	Std. Dev.	Skewness	Kurtosis	Jarque-Bera	Probability	Observations
U	0.00	-0.13	15.36	-15.31	3.30	0.18	5.26	524.02	0.00	2400.00
Y	5.48	5.96	8.09	-0.90	1.79	-0.59	2.66	148.73	0.00	2400.00
K	-0.03	-0.02	1.93	-1.80	0.55	-0.21	4.17	154.28	0.00	2400.00
CK	22.28	22.49	26.55	17.82	1.88	-0.04	2.14	73.95	0.00	2400.00
K	-0.10	-0.06	6.06	-7.45	1.44	-1.39	12.04	8945.06	0.00	2400.00
K	0.02	-0.01	2.24	-1.93	0.61	0.13	4.09	125.74	0.00	2400.00
N	0.09	0.21	2.30	-8.23	1.24	-2.05	12.00	9776.41	0.00	2400.00

Source: Authors’ Computation (2024)

The aggregative averages and measures of spread are shown for all the volatility series and the financial system stability indicator. The most significant interest is given to the measures of the normality of the series. The measure of peakness and the measures of symmetry as well as the Jarque Bera statistics all point to the leptokurtic nature of the series. The shocks are manifested by the fat tail and high peakness of the series.

The presence of time series properties in a longitudinal series such as the one we have in this study

makes unit root test imperative. The result of the test is of the form reported in table 2.

Table 2: Summary of Panel Unit Root Tests

	LLC	Breitung	IPS	ADF-fisher	PP-Fisher	Inf
BZSCOREVOL	-22.2419 (0.0000)	-18.0495 (0.0000)	-23.4461 (0.0000)	656.137 (0.0000)	1739.84 (0.0000)	I(0)
LEXRSHOCK	-22.8081 (0.0000)	-15.239 (0.0000)	-24.7753 (0.0000)	700.486 (0.0000)	1647.88 (0.0000)	I(0)
LGEXPSHOCK	-24.2162 (0.0000)	-18.4268 (0.0000)	-26.8588 (0.0000)	771.348 (0.0000)	1421.40 (0.0000)	I(0)
LGREVSHOCK	-24.0154 (0.0000)	-10.018 (0.0000)	-25.6506 (0.0000)	744.230 (0.0000)	1604.80 (0.0000)	I(0)
LGRTHSCHOCK	-21.3365 (0.0000)	-16.1512 (0.0000)	-24.1076 (0.0000)	681.443 (0.0000)	1591.04 (0.0000)	I(0)
LINTRSHOCK	-19.8784 (0.0000)	-13.6181 (0.0000)	-26.3556 (0.0000)	754.298 (0.0000)	1854.93 (0.0000)	I(0)
LPDEBTSOCK	-22.9076 (0.0000)	-15.1645 (0.0000)	-24.1379 (0.0000)	680.525 (0.0000)	1698.08 (0.0000)	I(0)
PRICESOCK	-22.5264 (0.0000)	-7.13462 (0.0000)	-24.5831 (0.0000)	708.378 (0.0000)	1376.01 (0.0000)	I(0)

Source: Authors' Computation (2024)

The test results follows the framework by Levin, Lee and Chu(LLC), Breitung, Im, Pesaran, Shin (IPS), ADF fisher and Philip Peron Fisher respectively. The use of multiple panel unit root test is to ensure robustness and reliability of the conclusions drawn from the tests. All the tests are consistent in reporting the stability and shock variables as being integrated of order zero. In all the test the null hypothesis of absence of unit root in the panel is rejected at levels which is symptomatic of I(0) variables for all the series.

Table 3 shows the linear association of financial system stability and the fiscal shock series in a panel correlation matrix.

Table 3: Panel Correlational Matrix

	BZSCOR EVOL	LEXRSH OCK	LGEXPS HOCK	LGRTHSC HOCK	LGRE VSHO CK	LPDEBTS HOCK	LINTRSHOCK N
LEXRSHO CK	0.0047	1.0000					
	0.2294	-----					

	0.8186	-----					
LGEXPSH OCK	0.0088	0.0325	1.0000				
	0.4305	1.5903	-----				
	0.6668	0.1119	-----				
LGRTHSC HOCK	-0.0429	0.0240	-0.0640	1.0000			
	-2.1021	1.1763	-3.1406	-----			
	0.0357	0.2396	0.0017	-----			
LGREVSH OCK	-0.0310	-0.0121	-0.0693	0.0788	1.0000		
	-1.5176	-0.5905	-3.4035	3.8695	-----		
	0.1292	0.5549	0.0007	0.0001	-----		
LPDEBTS HOCK	0.0262	-0.0290	0.0019	-0.0079	0.0703	1.0000	
	1.2825	-1.4204	0.0938	-0.3890	3.4526	-----	
	0.1998	0.1556	0.9253	0.6973	0.0006	-----	
LINTRSH OCK	0.0336	-0.0080	0.0472	0.0330	-	0.0707	-0.0881
	1.6483	-0.3938	2.3115	1.6144	-	3.4721	-4.3307
	0.0994	0.6937	0.0209	0.1066	0.0005	0.0000	-----

Source: Authors' Computation (2024)

The correlational matrix indicates that shocks from diverse fiscal indicators affect the stability of the financial system differently. For example, it can be observed that financial system stability shares a positive correlation with most of the fiscal shock indicators except for government revenue and growth. This is to say that shocks emanating from debt, interest rate, exchange rate and public expenditure share a positive co-movement with financial system stability; implying that such shocks are positively correlated with the stability of the financial system. For the shocks emanating from growth and revenue, a negative correlation is found. This means that there is evidence that shocks from growth and revenue move in opposite direction with the stability of the financial system.

Though the panel correlational matrix shows a degree of association and relationship among the investigated series, it does not suggest elasticity since the test is directionless.

Next, the responsiveness of financial system stability to the shock variables is shown in the dynamic panel least squares reported in table 4.

Table 4: Summary of Dynamic Panel Least Squares Results.

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LEXRSHOCK	0.009	0.034	0.274	0.784
LGEXPSHOCK	-0.460	0.114	-4.030	0.000
LGRTHSCHOCK	-0.212	0.033	-6.324	0.000
LGREVSHOCK	-0.140	0.045	-3.119	0.002
LPDEBTSHOCK	0.578	0.102	5.682	0.000
LINTRSHOCKN	0.468	0.052	8.991	0.000
Mean				
R-squared	0.0176959184719615	dependent var	0.004669556205358677	
Adjusted R-squared	-0.005453088	S.D. dependent var	3.31638438488799	
S.E. of regression	3.325414359822684	Sum squared resid	24870.29811449403	
Long-run variance	7.943720574123192			

Source: Author’s Computation (2024)

The result shows a low R-squared which is suggestive of a low level of multicollinearity of the stability series with shock variables. It implies that the series are independently and identically distributed.

There is an adverse impact from expenditure shock to the stability of the financial system. It is observed that a unit increase in shock arising from government spending reduces the stability of the financial system by a significant coefficient of 46%. This can be true of SSA countries with a high level of fiscal indiscipline and over bloated public spending which most times are on recurrent spendings that are not project-tied.

Shocks arising from growth and government revenue also showed to exert adverse effect on the stability of the financial system. It is common in SSA to see unbalanced growth which usually arises from increase in earnings from exportation of primary goods. This usually occurs as a result of increase in primary production without increase in growth of manufacturing and service sector. This lopsidedness will unsettle the service sector which predominates the financial system. Consequently, our findings observes that a unit increase in shocks from growth and government

revenue destabilizes the financial system by a highly significant 22% and 14% respectively.

Conversely, shocks arising from debt and interest rate showed to be positive and significant in their effect on the stability of the financial system. It is important to note the flow of funds through the financial system that domestic and external debts engenders can increase loanable funds at the disposal of the operators in the financial system. Such increased lending activity can improve earnings and the financial performance of the economic agents in the financial system thereby adding to the degree of the stability of the system. This is also seen with interest rate shocks that posts a positive and significant coefficient in its interaction with the stability of the financial system. The statistical evidence from our investigation shows that a unit increase in debts and interest rate shocks respectively and significantly stabilizes the financial system by 57% and 47%.

In sum, this study establishes a strong link of adverse and positive dimension between shocks from fiscal policy variables and the stability of the financial system in SSA countries.

5. Conclusion

This study was set to investigate the impact of fiscal shocks on the stability of the financial system in sub-Saharan African countries. The investigation is made necessary by the degree of fiscal dominance in SSA country at the detriment of monetary policy with the increasing debt profile and other inhibiting economic circumstances. The study focused on 45 SSA countries covering a 50-year period (1973-2023) with attention of significant episodic changes within the period.

Relevant econometric techniques were deployed to estimate the shock series obtained as the volatility series of the proxied fiscal policy indicators. Key empirical findings were documented from the relevant tests which represents the outcome of this study.

First, it was established that fiscal policy and the application of the associated indicators have been a source of intervening shocks to the financial system in SSA countries. This brings to fore the twin-policy application in managing SSA economies. Growth, government revenue, public debts, exchange rate and interest rate shocks were established to exist and have some effects of diverse dimensions on the stability of the financial system.

Second, it was found that public debt and interest rate shocks are favourable to the stability of the SSA financial system. The burgeoning debt profile of SSA countries creates shocks that significantly stabilize the system. This is same as the shocks from the diverse interest rate regimes in SSA countries. Revenue shocks, expenditure and growth shocks poses threat to the stability of the financial system and should be mitigated against through appropriate balancing of policy actions and the stabilization of the financial system.

This study provides a significant addition to the discourse on fiscal policy, dominance and their effects on the economic and finance space in SSA countries which makes it good enough for generalization for regions in the form of SSA countries.

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