The Impact of Fuel Subsidy Removal, Floatation of Exchange Rate and CBN Unbanning of 43 Items from Accessing FX on the Nigeria's Economy

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1. Introduction

Undeterred by the controversies and judicial contentions that trailed his election and swearing-in on May 29th 2023 as president of Nigeria, Bola Ahmed Tinubu, announcement of three bold economic policies of fuel subsidy removal, floatation of country currency exchange and unbanning of 43 prohibited items from accessing foreign exchange from the Central Bank is reverberating across the economic firmament of the country and potentially may define his administration. One of such policies was announced during his inauguration speech, 'subsidy is gone' (PWC, 2023). The statement was made in apparent bid to match his mantra of 'hitting the ground running', ostensibly to show that the new president is courageous and willing to tread the paths previous administrations were afraid to trod. The sudden removal of fuel subsidy led to spike in inflation on the economy and living condition of citizens (Ijioma, 2023). As if that is not enough, the new administration followed up with another major policy announcement, 'floating the naira exchange rate', so as to eliminate the wide disparity between official and black-market rates that has been the order of the day in Nigeria's foreign exchange markets for decades (Eromosele, 2023). But then the implication of allowing market forces to determine exchange rate have its own unique consequences for an import-dependent economy like Nigeria, thus multiplying the hardship resulting from subsidy removal (Englama et al, 2010). As Nigerians and the government were dillydallying on ways to cushion the negative impact of the already announced policies, the Central Bank (CBN), announced a reversal of its 2015 policy of prohibiting 43 items from accessing foreign exchange (Ebulu et al, 2023).

The combined effect of these treble major policies have had a profound effect on the Nigeria economy This article discusses the policies and it effects on the Nigerian economy.

2. The Fuel Subsidy Removal Debate in Nigeria

The regime of fuel subsidy crept into the Nigerian economy in 1977, when the then military administration of Olusegun Obasanjo promulgated the Price Control Act (Gwangwangwan, 2023). This act made it illegal for some products (including petrol) to be sold above regulated price to make them more affordable for the people. For petroleum products, it was argued that since Nigeria is the seventh largest crude oil producer in the world and has significant oil reserves, the citizens should enjoy the blessing of God. Moreso the government wanted to mitigate the impact of price fluctuation on cost of living to the citizens (Gwangwangwan, 2023).

But the cost of subsidizing petroleum products has been a major drain on government finances, leading to significant fiscal deficits and a strain on the country's budget (Adetayo, 2023). Furthermore, the subsidy regime has been beleaguered by corruption and inefficiency justifying. calls for its removal to redirect the funds saved towards critical sectors of the economy. The argument is that such action would encourage private sector investments in the oil sector (Chima, 2019). But voices against this course of action led by the Labour movement in Nigeria, have resisted implementation on the premise of its potential negative impact on the poor and vulnerable segments of society. They argued that removing fuel subsidy will results in significant increase in the price, which would have a cascading effect on the cost of transportation, food, and other essential goods and services. This, in turn, could aggravate poverty and inequality in the country (Yusuf, 2023).

Though debate of subsidy removal started in 1988, when Nigeria was still under military regime, the issue took a life of its own in 1999 when President Olusegun Obasanjo attempted to deregulate the downstream sector of the oil industry, including removing subsidies on petroleum products (Gwangwangwan, 2023). However, due to public resistance and protests, the plan was abandoned. Another bold attempt by President Goodluck Jonathan administration in January 2012, sparked widespread protests across the country, known as the “Occupy Nigeria” protests. Eventually, the government bowed to pressure and rescinded its decision (Chima, 2019). In May 2016, the President Muhammadu Buhari administration announced the complete removal of fuel subsidy. This led to a significant increase in fuel prices, which resulted in nationwide protests (Chima, 2019).

But the subsidy came back through what the national oil company NNPC tagged ‘under-recovery’. Even though the passage of Petroleum Industry Act (PIA) prohibited subsidy, the administration of Mohammadu Buhari continued payment until President Tinubu announced during his inaugural speech that ‘subsidy is gone’ (Dike, 2023). The government premised this action on the fact that about $5.2 trillion was spent on fuel subsidy alone since 2015 while World Bank report claim that in 2022 the amount stood at N731 billion (Dike, 2023). The question asked is why continuing the subsidy regime under an increasing cost and dwindling revenue by government as Nigeria is only able to produce 1.9 million barrels a day (mbd) against Organisation of Petroleum Exporting Countries (OPEC) quota of 2.3mbd (Chima, 2019).

While the concept of subsidy itself is noble, its administration in Nigeria has been plagued with serious allegations of corruption and mismanagement. Though subsidy on diesel and kerosene was removed in 2003 and 2016 respectively, subsidy on Petroleum Motor Spirit (PMS) has proven to be the biggest challenge to the managers of the Nigerian economy (Chima ,2019). On an annual basis, a substantial portion of the national income is committed to funding the subsidy scheme including borrowing that have increased the debt profile of the country to N 77 trillion (Faminu,2023).

3. The Floatation of Naira

In order to eliminate the dual exchange rate of the country’s currency, the Tinubu administration on Wednesday June 14, 2023, through the Central Bank of Nigeria (CBN) directed Deposit Money Banks (DMBs) to eliminate the rate cap on the Nigerian naira at the Investors’ and Exporters’ (I&E) Window of the foreign exchange market (ChapiOdekina,2023).

Floating exchange rate, refers to a monetary system where the value of a nation’s currency is determined by market forces such as supply and demand. For years CBN have pegged value of naira to major world currencies, thus creating two exchange rates, the official and the black market (Eromosele,2023). The disparity between the two provided an avenue for people with access to dollars and other convertible foreign currencies to buy at the official rate and resell at the black market. This distorted system ‘roundtripping’, has created many rich people with zero entrepreneurship (Adebowale,2022). However, the idea of floating the exchange rate is meant to solve this problem, but experts concede that it holds both potential advantages and risks.

Figure 1: Naira-Dollar Exchange, (Nairmetrics 2023)

4. **43 Prohibited Items on FX**

Beside the removal of fuel subsidy, and floating of the naira exchange rate, another major economic policy taken by the Tinubu administration is unbanning of 43 items from accessing foreign exchange (FX) from the I & E window. The CBN on 12th of October, announced the restoration of the 43 items to the official FX platform (Ebulu,2023). The decision was part of the policy normalisation process of the CBN, to improve transparency and erase distortions in foreign exchange transactions (Ebulu, 2023). The exclusion of the 43 items underscored the distortion in the forex market in turn, contributing to persistent divergence in rates between the official window and the parallel market. Experts have argued that the exclusion a trade policy which is outside the core mandate of CBN (Olayinka et al, 2023). More so, when the items were not under import prohibition.

It can be recalled that in 2015, the CBN restricted the availability of foreign exchange to the importation of 43 items which could be locally produced within the country. In June 2015, the Central Bank announced that some 41 items were "Not Valid for Foreign Exchange" because they could easily be produced in Nigeria rather than being imported into the country.

Some of the affected items include rice, cement, margarine, palm kernel, palm oil products, vegetable oils, meat and processed meat products, vegetables and processed vegetable products, poultry, tomatoes/tomato paste, soap and cosmetics, and clothes.

Other items include private aeroplanes/jets, Indian incense, tinned fish in sauce, cold rolled steel sheets, galvanized steel sheets, roofing sheets, wheelbarrows, head pans, metal boxes/containers, enamelware, steel drums and pipes, wire mesh, steel nails, wood particle boards, and panels.

Equally affected were security and razor wire, wood particle and fibre boards and panels, wooden doors, furniture, toothpicks, glass/glassware, kitchen utensils, tableware, tiles (vitrified, ceramics), textiles, wooden fabrics, plastic/rubber products, polypropylene granules, and cellophane wrappers (Eromosele, 2023). Fertilizer and maize/corn were later added to the list of banned items. But after close to eight years of implementing this policy which was aimed at stimulating local production of the listed items, the objectives behind it seem not to have worked hence the unbanning by the CBN. There are concerns on the implication of this policy reversal on the economy (Chapiodekina, 2023). However, importers of the 43 items are to advised to deploy the forex sourced by them from the cheaper official window into importation of raw materials and equipment rather than finished products so as to create jobs thereby strengthening the economy (Eromosele, 2023).

5. **Effects of Trebble economic policies on the economy**

The immediate effect of removal of fuel subsidy on May 29,2023 was 150% increases in pump price of petroleum motor spirit(pms) spiraling inflation of over 25% in the country particularly transportation costs and food items in the market (Adetayo, 2023). For example, fuel price jump from the official pump price of 185 naira ($0.40) to 550 naira ($1.18). The implication was widespread negative economic consequences on the Nigeria economy where 133 million people are living in multidimensional poverty. Unfortunately, the country has no working refineries, which means the cost of imported refined fuel would now be fully borne by consumers. Very ironic is that as fuel prices increased to a staggering 224 per cent, salaries of working Nigerians remained stagnant forcing vast majority to adjust their lifestyle (Adetayo, 2023). Though there are drop in average daily consumption of fuel by 28 percent the labour movement comprising Nigerian Labour Congress (NLC)and Trade Union Congress (TUC) threatened to embark on strike if government does not ameliorate the suffering of the masses (Ijaseun, 2023). The strike that would have shut down the country was averted by federal government promises of palliatives including cash awards to government workers, conditional cash to about 15 million vulnerable families and low interest loans to MSMEs (Ijaseun, 2023).

However, the floatation of the currency exchange multiplied the suffering following the crash in the value of the naira within few weeks of the policy. For instance, as at Monday October 23, 2023 the naira at the parallel market that was exchanging for N700/ $1 plunged to between N1,250-N1,300 (Nelson ,2023) even though the official rate which was fixed at N435 /$1 jumped to N800/$1(Nelson, 2023). The fall of the naira compounded the general inflation in the country as the price of imports into the country escalated. Even the pump price of fuel which rose sharply due to removal of subsidy continue to rise due to increase in the landing cost of fuel resulting from high exchange rate and rise in crude oil price in the international market (Englama et al, 2010; Bawa et al, 2020).

FX in Nigeria is an alluring arbitrage system given rise to existence of thriving black market as people prefers to keep their forex thereby creating an artificial scarcity. Consequently, CBN is unable to meet demands of forex. For instance, as at October 2023 the I&E window averaged $100 million in daily turnover (Adebowale, 2023). This explains the disparity of rates between black market and I & E window. Currently the CBN is unable to meet demands foreign airlines totaling about $783 million of their monies. Fitch Ratings of CBN has it that over $12 billion of payments are pending (Nelson, 2023). This pressure sustains the disparity between I & E window and black market even though the government attempted to stabilize the rate through a $3 billion crude oil swap loan from Afreximbank (Adebowale, 2023). Beside impact on consumers, businesses are also experiencing downturn in their operation due to reduction in purchasing power.

Manufacturing companies that depend on imported raw materials for their operation have experiencing rise in cost of operation and reduced profit margins (Olayinka et al, 2023). The unstable FX is not only affecting inflow of investment from foreign companies but diaspora investment which ought to be boosted with low naira exchange rate has not improved because of the instability in the FX market (Nelson, 2023).

The other major economic policy, unbanning of 43 items prohibited from accessing FX from official window is also having effect on the economy. Local manufacturers and farmers in the country have expressed fears that the unbanning of 43 items initially placed on the foreign exchange prohibitive list by the Central Bank of Nigeria (CBN) is capable of sending many of them out of business (Chapiodekina. 2023). idea behind lifting the ban on the 43 items was to reduce the pressure in the black market and increase liquidity through the official route, where exporters would be able to buy and sell forex at the I&E window instead of the unofficial market. Indeed, the idea behind the ban initially was to manage the scarce forex and protect local manufacturers by making the import of those items quite expensive and unable to compete with locally manufactured products.

5.. Conclusion

The controversy and judicial contention that surrounds the election and swearing in of Bola Ahmed Tinubu as president of Nigeria has imbued the administration with deficiency of legitimacy that the regime was bent on courting an image of strong leadership that is not afraid to take bold decision. The treble major economic policies of the less than seven months old administration of the new president is nothing short of the obvious. The treble policies of fuel subsidy removal, floatation of currency exchange rate and unbanning of prohibited item from accession forex on face value are laudable and bold, but the manner of implementation in the light of dynamics and fundamentals of the Nigerian economy matters a so much on how it will impact on the economy. The short-term implication has created an economic crisis that is negatively impacting on Nigerians and their economy, however the administration's doggedness and determination to continue with the policies may turn out positive in the long run for Nigerian economy.

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