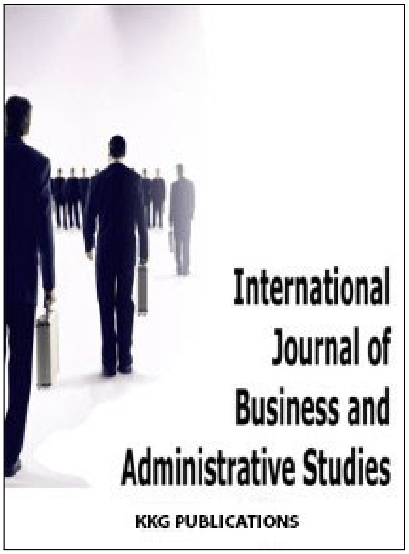

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THE ECONOMIC IMPLICATION OF FUEL SUBSIDY REMOVAL IN NIGERIA

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Abstract. This study investigates the economic implications of the removal of fuel subsidies in Nigeria. As an economic discourse, it addresses the arguments for and against the removal of fuel subsidies in Nigeria. This paper observes the growing public opposition to the elimination of fuel subsidies. It was discovered that the sector was characterized by gross corruption, abuse of office, inadequate record-keeping, insufficient supply, smuggling and inefficiency. The paper also examines various regimes of fuel price increases, subsidy payments and their effectiveness or otherwise in stimulating economic activities in Nigeria and makes recommendations on the need to build more refineries to make the product more available to the people at an affordable pump price. In the short run, the fuel prices would go up significantly but would drop when the products of the new refineries are released into the market. Also, the paper recommends that for the smooth operation of the petroleum sub-sector, the government should always engage the people in policies that will affect them.

INTRODUCTION

Nigeria is blessed with vast quantities of petroleum resources and is the sixth largest oil exporter in the Organization of the Petroleum Exporting Countries (OPEC). This has generated billions of dollars in revenues over the last fifty years since oil was discovered in Nigeria. However, this has not translated into an improved welfare condition for the people largely because of corruption, mismanagement, inefficiencies, smuggling, bureaucratic bottlenecks and excessive subsidizing.

For five decades now, Nigeria's economic policies, growth and other related activities have been to a large extent influenced by the oil industry is an understatement as the oil sector is a life-blood for the Nigerian economy (Adelabu, 2012). Available evidence in literature shows that Nigeria is the largest in Africa and the sixth largest oil producing country in the world. Despite these developments, successive Nigerian governments have been unable to use the oil wealth to significantly reduce poverty, provide basic social and economic services for her citizens' needs (Ering & Akpan, 2012).

Subsidy has many interpretations. It may be an assistance paid by government or only measure that keeps prices consumers pay for product or good below market levels. Subsidy means benefit given by the government to individuals or businesses whether in form of cash, tax reduction or by reducing the cost of goods and services. The purpose of subsidy is to help individuals and businesses purchase/acquire essential goods or service that they may not be able to afford under normal circumstances.

Subsidies take different forms; these include grants, tax reduction or by reducing the cost of goods, exemptions or price controls. Others affect prices indirectly such as regulations that skew the market in favor of a particular fuel, government sponsored technology or research and development (Adebiyi, 2011; Del Granado, Coady, & Gillingham, 2012). Fuel subsidy means that a fraction of the price that consumers are supposed to pay to enjoy the use of petroleum products is paid by government so as to ease the price burden. Fuel subsidy is a form of price manipulation whereby the government fixes the pump price of fuel for sale to consumers and pays the retailer the difference between the actual price and the regulated or official price per litre (Iyobhebhe, 2011; Nwafor, Ogujiuba & Asogwa, 2006).

Statement of Problem

Nigeria is a large net importer of gasoline and other petroleum products despite being blessed with vast quantities of crude petroleum resources. This has resulted into the depression of Nigeria's international financial markets, Nigeria's foreign exchange rates continue to show weakness, naira posting a persistent slide against all major currency. Unemployment rate is becoming alarming. Most industries are closing down because of their inability to cope with the business challenges (Onyeizugbe & Onwaka, 2012).

In spite government effort to revamp the economy through non-oil export diversification drives, petroleum still contributes over 90% of Nigeria's external earnings. Nigeria is increasingly relying on imported petroleum products while the existing four

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refineries are producing less than 30% of their installed capacity. In fact, the cost of importing petroleum products has increased so rapidly in recent years that is threatening the country's balance of payments and capital expenditure (Adelabu, 2012).

Government control of petroleum product prices has been a major issue before now, especially in the face of the failure of the government to get existing refineries to full capacity utilization. Investors, who had wanted to invest in the establishment of refineries were scared away by what they saw as unfriendly pricing, leaving product marketers with low or no margins, except when government stepped in with a heavy subsidy that ate deeply into its treasury (Balouga, 2012).

ECONOMIC IMPLICATIONS OF FUEL SUBSIDY IN NIGERIA

Fuel crisis has become the order of the day in Nigeria despite being richly endowed with large crude oil deposit. It is pathetic to observe that no other OPEC member or even country that does not produce oil, shares similar ugly experience with Nigeria (Badmus, 2009). In economic sense, subsidy exists when consumers of a given product are assisted by the government to pay less than the prevailing market price by the government that is caused by import induced costs. These costs according to Afonne (2011) have been discovered to be responsible for the high prices of petroleum products in Nigeria. Fuel subsidy was before the coming of Jonathon administration, a policy of government to assist the people of Nigeria to cushion the effects of their economic hardship.

Nigerian oil and Gas downstream sector is dominated by cartels who manipulate prices through artificial restriction of supply. These cartels determine volume of importation and the proportion that should be released to the market. Peter Akpatasan, President of NUPENG has stated thus: "Deregulation cannot work in market dominated by cartels. These cartels are so strong that it can continue to manipulate prices out of the reach of common man. You cannot deregulate when you have no refineries. There will be serious economic crisis".

Nigeria's four refineries have a maximum installed capacity to process 445,000 barrels of crude oil per day. This is less than 40 percent of the daily domestic consumption requirement. Such a low production capacity is further encumbered by maintenance and operational lapses which resulted into inevitable severe product shortages, the situation is further worsened by the price disparity between Nigeria markets and her sub-regional neighbors, which encourages product smuggling and further widens the gap between supply and local demand. The history of petroleum subsidy removal in Nigeria is rather a long one as table below:

TABLE 1
Petroleum Subsidy Removal in Nigeria

S/NO	Date	Administration	Price	Percentage change
1.	1978	Obasanjo	15k	—-
2.	1990	Babangida	60k	300%
3.	1992	Babangida	70k	17%
4.	1992	Babangida	N3.25	364%
5.	1993	Babangida	N5.00	54%
6.	1994	Shonekan	N11.00	120%
7.	1994-1997	Abacha	N11.00	—-
8.	1998-1999	Abacha	N20.00	82%
9.	2000	Obasanjo	N20.00	—-
10.	2000	Obasanjo	N22.00	10%
11.	2001	Obasanjo	N26.00	18%
12.	2003	Obasanjo	N40	54%
13.	2004	Obasanjo	N45	13%
14.	2007	Obasanjo	N70	56%
15.	2007-2009	Yar'adua	N56	0.0%
16.	2010-2012	Jonathan	N65	—-
17.	2012	Jonathan	N145	117%

The Petroleum Products Price Review Agencies (PPPRA) had been regulating the selling prices of fuel. It reimbursed the differential between the unprofitable prices the importers of petroleum products sell to the public. Below is the template prepared by PPPRA daily and monthly.

Import Landing Cost (N/ litre)	Marketers Markup Margin (N-/ liter)	Expected Open Market Price (N/litre)	Approved %Retail Price (N-/litre)	Govt. Subsidy (N-/litre)	Dealers Official Profit (N-/litre)	Markets Price (N-/litre)

Source: PPPRA Release

A lot of money had been removed as petroleum subsidy in Nigeria through persistent increase in petroleum products prices by government. Each administration had initiated programs for the utilization of the removed subsidy for the benefit of poor which included, Babangida's Directorate for Food, Roads and Rural Infrastructure (DFFRI 1986), Vision 2010 (Aluko, 2006) and Obasanjo's Program 2016. According to Obasanjo, fuel price increase does not translate into poverty but the non-judicious use of additional revenue that accrued there from. He continued to list the following indicators of poverty as lack of health care delivery, lack of potable water, lack of education for children and lack of good roads, he promised to channel fund accrued from subsidy removed to address the listed areas of the economy and the rehabilitation of refineries, (Simon-Reef, Ojeme & Owolabi, 2005).

With the increase of fuel price in 2012, the Jonathan administration established the Subsidy Reinvestment and Empowerment Program (SUREP, 2012) with the objective of stimulating the economy and alleviate poverty through development of critical infrastructure that would transform the economy. However, the objective had not been achieved. Fuel scarcely had been persistent resulting in long queries, wasted man-hours on queries, fuel adulteration resulting in fire incidences and the consequent loss of lives and loss of production. Despite all these, investment in the downstream had not been stimulated as local refineries have been at low capacity production, poverty as well had increased among the people. Based on the above, the implications of fuel subsidy on Nigerian economy are as follows:

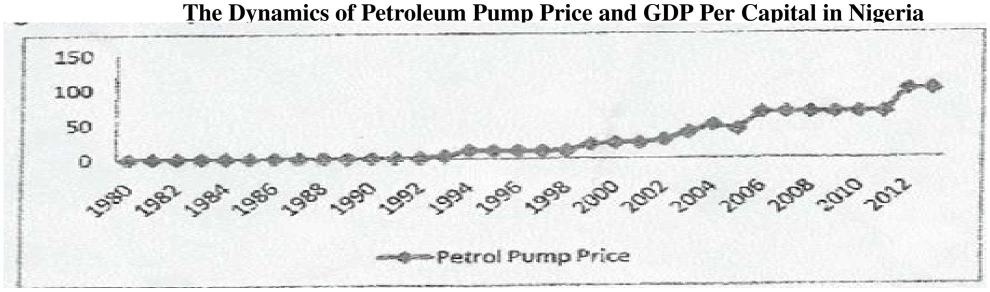
- Lack of clear and quantifiable plans of government on the utilization of removed subsidy of most of items listed to be financed in the SURE program were mere political statements. Dissatisfied with implementation and the lack of transparency in the utilization of the removed subsidy, the Governors of the 19 Northern states resolved to ask the federal government to explain what it was doing with the oil subsidy money (Umaru, 2013).
- Absence of records of the actual cost of subsidy, production output of refineries and national fuel consumption.
- Price regulation regime of government had weakened investment in the petroleum sector.
- PPPRA's markup margin for markets and dealers were arbitrarily determined to give supernormal profit to importers.
- Deficiencies of subsidy payments sabotage local refineries operators.
- Fuel marketers involved in the diversion of subsidized fuel across borders with a devastating consequences of creating scarcity of fuel in the domestic market for their personal gain.
- The low price of fuel products encourages excessive and inefficient usage of fuel.
- Absence of competitive market price discourages entry of private investors.
- The large price differential between price in the domestic market and Nigeria's neighboring countries encourages smuggling for profit thus depleting local supply.

Petroleum Price and Nigerian Economy

The table below shows the movement of the pump price of petroleum from 1980 to 2012 as well as the income dynamics in the Nigeria economy.

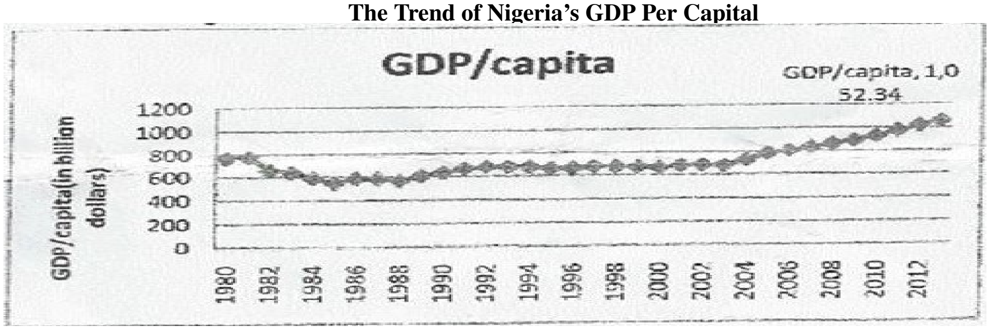
FIGURE 1

The Dynamics of Petroleum Pump Price and GDP Per Capital in Nigeria



Source: NNPC (2008, 2009, 2010, 2012); PPPRA (2006)

FIGURE 2
The Trend of Nigeria's GDP Per Capital



Source: World Bank

From the figure above, it can be observed that price of fuel has been rising steadily in some years. In 1980 the pump price was 5k, and by the end of the SAP era, the fuel price had moved to 70k in 1992, in 1993 the price shot to N5 before reducing to N3.75 after several protests. At Abacha regime, the pump price stood at N20 from previous N11 and in 2002, the price shot to N26 and N65 in 2006. On January, 2012, the pump price of petroleum was increased to N141 rising by whopping 117 per cent before being reduced to N97.

On the other hand, the GDP per capita has shown remarkable increase over the past 3 decades, although the growth rate of per capita GDP has not been significant. The reason for this slow growth rate has been attributed to the effect of oil glut of the early 80s, the inefficiency of the SAP, political instability that has engulfed the nation, the issue of corruption and various policy mismatches by the government.

RECOMMENDATIONS

Government should partner with the major oil companies like Chevron, Shell BP and Total to build more refineries in Nigeria and at the same time fast tracking the turnaround maintenance of the refineries.

The Nigeria government must put in place transparent system for monitoring the use of fuel subsidy program so that citizens could review and scrutinize expenditure.

Fuel subsidy removed should not be an instant decision without palliative measures like making the power sector more effective. This would reduce burden of subsidy removal on the people.

Government should regulate the activities of fuel marketers and some unscrupulous elements in the petroleum marketing that sabotage the efforts of government by creating artificial scarcity for personal benefits.

Policies towards achieving long term economic growth and development should be formulated and implemented by channeling the proceeds of fuel subsidy to invest massively in infrastructural development.

Government should also assemble a consortium of experts irrespective of political affiliation to address modalities for the deregulation of the downstream petroleum sector.

CONCLUSION

Nigerian government had for many years been removing subsidy. Every removal of subsidy and announcing had generated protest from the people because of the Negative impact on the people. The question is that whether the government is simply interested in removing subsidy so as to channel the proceeds from subsidy removed to finance other projects or to deregulate the petroleum industry in order to stimulate investments and create jobs.

The local producer would not be able to supply its products into the same market whose imported petroleum product is subsidized and therefore deregulation of the petroleum downstream would attract investors to build and operate refineries.

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