

Chapter 7

Implications of Fuel Subsidy Removal on the Nigerian Economy

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ABSTRACT

The purpose of this chapter is to discuss the implications of the 2023 fuel subsidy removal in Nigeria. Using the discourse analysis methodology, the authors offer some insight into the macroeconomic and microeconomic implications of the 2023 fuel subsidy removal in Nigeria. The positive implications are that fuel subsidy removal would free up financial resources for other sectors of the economy, incentivize domestic refineries to produce more petroleum products, reduce Nigeria's dependence on imported fuel, increase employment, channel funds for the development of critical public infrastructure, reduce the budget deficit and generate a budget surplus in the near future, reduce government borrowing, curb corruption associated with fuel subsidy payments, increase competition, reinvigorate domestic refineries, and reduce pressure on the exchange rate.

1. INTRODUCTION

Fuel subsidy is a government discount on the market price of fossil fuel to make consumers pay less than the prevailing market price of fuel (Ovaga and Okechukwu, 2022). When subsidies are in place, consumers would pay below the market price per litre of the petroleum product. Globally, there are debates about fuel subsidy because of its huge amount and its effect on citizens welfare and the fiscal health of a nation.

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The size of global fossil fuel subsidy is large and is estimated at \$1 trillion in 2022 from \$325 billion in 2018, according to the International Energy Agency. This amount is significantly higher than the value of global aid which was estimated at \$204 billion in 2022 and larger than the combined government revenue of developing countries. This has led to calls for the removal of global fossil fuel subsidy so that the saved funds can be channelled to assist the poor and vulnerable in need of humanitarian assistance in developing countries (Couharde and Mouhoud, 2020; Ozili and Ozen, 2021). However, the removal of fossil fuel subsidy is contentious because there is the argument that fossil fuel subsidy is a form of aid because it makes fuel more affordable for the poor. Despite this favourable argument, a large literature documents the negative consequences of fuel subsidy which include increasing air pollution and greenhouse gas emissions (Sweeney, 2020), road congestion (McCulloch, Moerenhout and Yang, 2021), road accidents and premature deaths (Parry, Black and Vernon, 2021), foregone tax revenue (Sweeney, 2020) and it increases inequality between the poor and the rich (McCulloch, Moerenhout and Yang, 2021). However, policymakers in many countries are reluctant to remove fuel subsidy and to implement fuel subsidy reforms because such reforms may result in a significant increase in fuel or electricity prices which could lead to economic hardship for low-income and poor citizens, and might lead to massive protest and increase the risk of a revolution or the overthrow of the incumbent government.

In Nigeria, fuel subsidies were first introduced in the 1970s as a response to the oil price shock in 1973. Fuel subsidies were partially removed in 1986. Since then, the fuel subsidies have been in place. In 2012, the government abruptly removed fuel subsidy. The removal led to massive protests which was intended for the government to reinstate the fuel subsidy it had removed. The government subsequently reinstated fuel subsidy in 2012 due to the massive protests. Since then, fuel subsidy payment in Nigeria has grown enormously. In 2022, fuel subsidy reached ₦4 trillion (US\$6.088 billion) which amounted to 23 percent of the national budget of ₦17.126 trillion (US\$25.87 billion) in 2022. As a result, Nigeria could no longer sustain fuel subsidy in 2023, and the government announced that fuel subsidy would be removed in June 2023.

Recent evidence in the Nigerian literature shows mixed effect of fuel subsidy. Some studies identify some benefits of fuel subsidy and call for transparency in the administration of fuel subsidy while other studies highlight the negative consequences of fuel subsidy and advocate for its removal. For example, Omitogun et al (2021) show that the removal of fuel subsidy might reduce the amount of carbon emission in the Nigerian economy. Similarly, Adekunle and Oseni (2021) argue that fuel subsidy removal could reduce the growth in carbon emissions through low energy consumption channels even though it could lead to higher energy prices. Asare et al (2020) argue in support of fuel subsidy removal and that the revenue gained from removing fuel subsidy could provide additional resources for the government to respond with immediate interventions to address the COVID-19 crisis and enable the government to shift resources into more productive spending for long-run post-COVID recovery and resilience (Ozili and Arun, 2023). Other studies highlight the consequence of fuel subsidy removal. Umeji and Eleanya (2021) argue that Nigerian oil wealth has not translated to improved standard of living despite the introduction of fuel subsidy, and that fuel subsidy removal could have severe consequences which can be mitigated by transparency on the part of government in spending the funds saved from fuel subsidy removal for infrastructural development. Also, Ovaga and Okechukwu (2022) argue that fuel subsidy breeds corruption in Nigeria because a group of corrupt people have been working against the functioning of existing refineries and they undermine efforts to build new refineries in Nigeria so that fuel importation would be sustained and fuel subsidy would be retained for the purpose of satisfying their selfish desires. Omotosho (2020) points out that fuel subsidy removal could lead to higher macroeconomic instability

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