

Chapter 7

Exchange Rate Unification in Nigeria: Benefits and Implications

Peterson K. Ozili

 <https://orcid.org/0000-0001-6292-1161>

Central Bank of Nigeria, Nigeria

ABSTRACT

This chapter explores the recent unification of exchange rate in Nigeria. Recently, Nigeria unified the exchange rate and adopted an imperfect free float exchange rate system that is based on the willing buyer willing seller principle. The exchange rate regime is slightly close to a free float exchange rate system. Multiple factors led to exchange rate unification in Nigeria such as exchange rate price arbitrage and the market distortion it created. The unification of exchange rate is expected to yield potential benefits such as fewer government intervention in the foreign exchange market, improve price discovery, greater foreign exchange supply, higher capital importation, reduction in budget deficit, increased investor confidence, improved sovereign credit rating, increased transparency in the foreign exchange market, improved business environment and greater competition. Adverse effects are expected in the short-term, but these effects will dissipate in the medium to long-term.

1. INTRODUCTION

Just like many developing countries, Nigeria has a long history of economic reforms. The most notable economic reforms are the 1986 structural adjustment programme (SAP), the 2003 Nigerian Economic Empowerment Development Strategy (NEEDS), and the 2023 exchange rate unification reform. This article focuses on the 2023 exchange rate unification reform.

The Central Bank of Nigeria (CBN) introduced multiple exchange rates under the managed float exchange rate regime between 2014 to mid-2023. The purpose of the multiple exchange rates was to allocate foreign exchange to exporters and SMEs under different foreign exchange rate windows such as the CBN exchange rate window, the Investor & Exporter (I&E) exchange rate window, and the Bureau

DOI: 10.4018/979-8-3693-2683-1.ch007

de change (BDC) exchange rate window during between 2014 to 2022. This exchange rate system had positive and negative effects on the Nigerian economy. It was abandoned in mid-2023 following the unification of all exchange rates by the President Tinubu Administration. The exchange rate unification reform of 2023 was intended to unify all exchange rates into a single market-determined exchange rate to promote transparency and price discovery in the foreign exchange market, among other benefits.

Nigeria is not the only country to unify exchange rate. Countries like Cuba, Australia, Canada, Chile, Japan, Mexico, Norway, Poland, and Sweden have also unified exchange rate. The literature report mixed effect of exchange rate unification on the economy of countries that have unified exchange rate (see, for example, Sanusi, 2010; Parvin and Banouei, 2020; Fleming, 1971; Kim, 2003; Sundararajan, Lazare, and Williams, 1999; De la Torre and Ize, 2013), and these studies suggest that the effect of exchange rate unification on countries is country-specific and is dependent on each country's economic fundamentals, economic policies, and implementation. In the case of Nigeria, it is difficult to determine the exact impact of exchange rate unification because Nigeria unified exchange rate at a time when the country was experiencing high inflation, large balance of payment deficit, large budget deficit, high government borrowing, high energy prices due to fuel subsidy removal, low government revenue and low foreign exchange (FX) supply. These unfavourable economic fundamentals may affect the success of the exchange rate unification process in Nigeria. Notwithstanding, economic analysts have begun to predict the potential effects of exchange rate unification in Nigeria. In this paper, I identify the potential benefits and implications of the unification of exchange rate in Nigeria and argue that the success of exchange rate unification will depend largely on effective implementation, sound economic policies, and the roll out of proactive measures to address any potential challenges or risks associated with exchange rate unification.

This article contributes to the literature in the following ways. First, it contributes to the economic literature that examine the effect of exchange rate reforms on economic performance (e.g., Zhang, 2000; Twarowska, 2019; Omojimite and Akpokodje, 2010). Second, the study contributes to the literature that examine the effect of central bank actions on markets (e.g., Lubik and Schorfheide, 2007; Aguilar and Nydahl, 2000; Beine, Lahaye, Laurent, Neely, and Palm, 2007). Third, the study contributes to the literature that examine the role of free markets in resource allocation. The present study contributes to this literature by identifying the potential effect of a market-determined exchange rate on foreign exchange allocation (e.g., Aliber, 2019; Jiang and Wu, 2022; Fatin and Wijayati, 2023).

The rest of the study is organized in the following way. The literature review is presented in section 2. A concise summary of Nigeria's exchange rate regimes is presented in section 3. The benefits of exchange rate unification are identified in section 4. Section 5 presents the implications of exchange rate unification in Nigeria while the conclusion is presented in section 6.

2. LITERATURE REVIEW

Gray (2021) clearly showed that a parallel market emerges and develops when the central bank's foreign exchange supply is unable to meet legitimate demand for current account transactions at the official exchange rate. Gray analysed the exchange rate unification in Algeria, Argentina, Burundi, Ethiopia, Lebanon, Nigeria, Sudan, South Sudan, and Venezuela, and found that when the spread between the official and parallel market exchange rate is both substantial and sustained, the price levels in the economy would reflect the parallel market exchange rate, not the official exchange rate. Gray further show that

7 more pages are available in the full version of this document, which may be purchased using the "Add to Cart" button on the publisher's webpage:
www.igi-global.com/chapter/exchange-rate-unification-in-nigeria/342390

Related Content

Explaining That Everything Trendy and New Is Essentially Slightly Changed Classics; Also Explaining How Leadership Can Be Maintained Using Traditional Means Under Non-Traditional Market Relations

(2018). *Regulation and Structure in Economic Virtualization: Emerging Research and Opportunities* (pp. 30-70).

www.irma-international.org/chapter/explaining-that-everything-trendy-and-new-is-essentially-slightly-changed-classics-also-explaining-how-leadership-can-be-maintained-using-traditional-means-under-non-traditional-market-relations/196342

An Empirical Study on Solar Performance, Cost, and Environmental Benefits of Solar Power Supply

Samreen Muzammil, Sarmad Ali Akhundand Faizan Channa (2022). *International Journal of Circular Economy and Waste Management* (pp. 1-23).

www.irma-international.org/article/an-empirical-study-on-solar-performance-cost-and-environmental-benefits-of-solar-power-supply/302203

Sustainable Logistics Systems: A Conceptual Paper

Zhang Yu (2021). *International Journal of Circular Economy and Waste Management* (pp. 41-48).

www.irma-international.org/article/sustainable-logistics-systems/281612

Mann Deshi Foundation: Model for Women Empowerment Through Human Capital Formation and Development

Minakshi Balkawade (2020). *Wealth Creation and Poverty Reduction: Breakthroughs in Research and Practice* (pp. 971-991).

www.irma-international.org/chapter/mann-deshi-foundation/241111

Ubuntu and Afrocentric Community Development for Community Development Practitioners in Working With Unemployment and Intergenerational Poverty

Kefilwe Johanna Dithake, Mamodise Mailulaand Sbusiso Thabane Mkhonza (2026). *Intergenerational Transmission of Youth Poverty and Unemployment* (pp. 365-386).

www.irma-international.org/chapter/ubuntu-and-afrocentric-community-development-for-community-development-practitioners-in-working-with-unemployment-and-intergenerational-poverty/413597