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THE IMPLICATIONS OF DWINDLING OIL PRICES ON THE NIGERIAN ECONOMY

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ABSTRACT

The main objective of the study is to ascertain the implications of dwindling oil prices in the Nigeria economy. This study adopts descriptive statics such as mean and standard deviation and inferential statistics which include Regression and Correlation analysis. Operational variables used in this study are gross domestic product (GDP) as a measure of national productivity and crude oil, industrial/services products, and capacity utilization. The study thereby concluded that dwindling oil price indicators significantly influence Nigeria Economic Development within the study period and that dwindling oil price and Nigeria economy exhibit significant relationship within the study period. In the light of the above findings, the study recommends that the Government should give a clear economic policy direction to develop and assist key financial industry players in stabilizing the financial economy. Also, the budget should be built based on the prevailing economic realities occasioned by the oil price fall to ensure prudency and accountability and to discourage wasteful allocation of the meager resources to non-productive expenditures.

Keywords: Oil price fall, Banks, Economy, Financial crisis, Diversification, Economic policy

Introduction

First and foremost, Nigeria is endowed with vast resources including such minerals as petroleum, limestone, tin, natural gas and others (Adeoye, 2005). All these minerals have remained untapped, except petroleum which has dominated Nigeria‘s economy since the 1970s. Today, petroleum is by far the most widely used energy resource worldwide. Its production and distribution, according to Aliyu, (2016), affects the relations among nations and even the purchasing power of some individual citizens. The first discovery of oil in commercial quantity in Nigeria was made in 1956. Shell-Bp was the principal company undertaking oil exploration and production activities in the country, although there were sporadic explorations by other companies, prior to that date

In addition, according to (Habib, 2014) the Nigerian government did not embark on serious oil policies for the country until 1967. The rapid inflow of oil revenue to the country in the early 1970s, led to the complete abandonment of agriculture which was Nigeria‘s economic mainstay. It was observed that since the beginning of oil production in commercial quantity, Nigeria has been rated high, the world over, such that she is declared Africa‘s second largest producer after Libya, eight largest exporter in the world and the worlds tenth largest oil reserves (Olomola, 2014).

Since Nigeria‘s export of first crude oil in 1959, it has become the major contributor to the country‘s economy, and that is why over 80% of the country‘s foreign exchange earnings come from the oil sector. Nigeria has been enjoying consistent increase in the revenue from oil. For instance, a barrel of oil was sold at 3.00 dollars per barrel in 1971, 12.42 dollars and 37.00 dollars a barrel in 1971 and 1980 respectively. Following steady increases in the sales, receipts swelled as well from 300 million dollars in 1970 to 4.2 billion dollars by the end of 1974, when oil production was 2.3 million barrels per day (Chris, 2016).

The oil sector is a key sector in the Nigerian economy. This is because; the revenue from oil is the major growth factor in the Nigerian economy. Resources generated from it, fund virtually all capital expenditures in the Nigerian system. The oil sector is closely linked with the financial sector, because the financial sector in every country is the oil which fuels the economy of such country and the bedrock for the sustenance and continuity of the sovereignty of a country. The impact of the oil price fall is disastrous on the Nigerian economic system; consumers are feeling the hit through escalating price of goods and commodities, massive sack of workers in the labor force among others. Therefore, there is a need for the Nigeria state to look inwards amidst the abundance of its untapped natural resources to diversify the economy of the nation, and increase export with a view to checkmating the insidious impact of the oil price fall on the economy (Sanusi, 2013)

1.2 Statement of the Problem

Nigeria economy is almost singularly hinged on crude oil export and therefore, highly sensitive to internal and external market shocks in the oil sector. What this means is that a fractional rise in cost of fuel has unmitigated ripple effect on the industrial sector and key components of basic need indicators such as food, housing and health. Secondly, the ripple effects are without boundary as social liberties for example, become less accessible to the average Nigerian and well removed from the less privileged who consist the vast majority of the over 145 million population. If Nigeria should borrow a leaf from these nations and allow the downstream sector to be fully deregulated, we are sure to have a success story to tell. Otherwise, Nigeria becomes an on-looker in the polity of oil producing nations (Obasi, 2014).

As the recent event unfolds, dwindling oil prices becomes inevitable. There is no point running away from grasping reality, efforts should instead be made to face challenges stoically. It is of a paramount importance that petroleum tax be implemented because it is a must food to be eaten one day. Nigeria's daily fuel imports went down 45 percent in 2016 or by 27 million litres a day, on the back of the partial removal of petroleum subsidies by the Federal Government. Meanwhile government is said to have borrowed N850 billion in 2016 to import products. A look at the pricing template of the Petroleum Pricing Regulatory Agency (PPPRA) for PMS for December 2016 showed that the landing cost of a litre of petrol is N124.76 while the distribution margin for transporters, retailers, bridging fund, marine transport average (MTA) and administrative charge is put at N15.49. This however brought the total cost of petrol to N140.25.

Meanwhile, when the initial official pump price was N97 per litre, the government is said to subsidize the difference of N43.25. Most of the scholars were talking about how subsidy removal will lead to employment, some are of the opinion that it would bring hardship and others were talking about the inflation rate.This study therefore, shall explore the strengths and weaknesses of dwindling oil prices in the Nigeria economy.

Objectives of the Study

The main objective of the study is to ascertain the implications of dwindling oil prices in the Nigeria economy. Other specific objectives of the study include:

1. To determine the effect of dwindling oil prices in the Nigeria economy

2. To ascertain if there is any significant relationship between dwindling oil prices and the Nigeria economy

Research Hypothesis

The following hypothesis is to be stated in null and norm form. The research will focus on this hypothesis, which may lead to rejection or acceptance.

H_0: There is no significant relationship between dwindling oil prices and the Nigeria economy

H_1: There is significant relationship between dwindling oil prices and the Nigeria economy.

Literature Review

The Impact of oil price fall on the Nigeria economy.

The oil crisis has been around for sometimes, the two oil crises in 1973 and 1979 are evidences of its persistent prevalence. To forestall the oil crisis, Organization of the Petroleum Exporting Countries (OPEC) was formed in September 1960 to regulate oil pricing between member state signatories, which became effective in 1973.6Nigeria became a member of OPEC in 1971.7 However, in recent times, they have been flurry of arguments as to the possible cause(s) of the oil price fall; some commentators had noted that it arose from US refinery maintenance, OPEC inaction, infiltration of global oil production by oil countries that are not part of OPEC,8 and the untoward activities on some country members of OPEC (Obasi, 2014)

Clearly, blame games are being traded daily by the oil industry players and oil nations as to who is to blame for the price fall and the possible causes of the oil price fall, with the solution farfetched. However, what is glaring to the global economy is the fact that the oil price had fallen and still on a steady decline. Failure to come up with a timeous holistic approach to solve the global oil price fall can affect countries and put their economy in bad shape. This oil price fall has affected the Nigerian economy in a huge way. To stem the tide of the oil price fall on the Nigeria economy, the current Central Bank of Nigeria (CBN)'s Governor, Godwin Emefiele, who was appointed in 2014, embarked on rigorous banking sector reforms to steady the economy. For example, to ensure an adequate regulation of the financial sector, the Central Bank of Nigeria in a report released on 30 October 2015, but reported on the 21th November 2015, directed three commercial banks to recapitalize after they failed to hit the minimum capital adequacy rate of 10% before June 2016 or risk being liquidated (Ogundipe, 2014).

The three commercial banks, where however not named to avoid bank rush on the current accounts of such banks. Furtherance to that report, the CBN also reiterated its commitment to monitor the re-capitalization plans of the three commercial banks. This is a reasonable and ingenious approach, because naming the commercial banks could cause a stare at other banks as well and such attitude could have a chain reaction on the already tensed and volatile financial sector in Nigeria. Also, monitoring the implementation plans of the three banks are commendable and encouraged, because, only adequate reforms and enforcement of regulation can stabilize, strengthen and secure the Nigerian banking sector in the current oil price fall.

Similarly, financial scandals are also identified as one of the impacts of the oil price fall on Nigerian economy. This is because; companies will be looking to maintain their luxurious lifestyle during the oil price steady and also during the oil price crash era. This will encourage the directors and executives of such firms to carry out activities contrary to the firms' policies. Notable in Nigeria, is the recent one being the AFREN Oil and Gas Company which had led to the firm sacking its Executive Directors and subsequently being put into administration. The oil price fall provides the leeway for such executives to fiddle with companies accounts, to assign huge bonuses to themselves and their cronies.

The oil price fall crisis incidence had in fact affected the Nigerian economy by causing paucity of funds for financial services. Recently, it was revealed by the banks, that several oil marketers owed some Nigerian banks to the tune of about ₦5 trillion. This is disastrous to the financial balance sheets of the affected banks, and could subject them to credit crunch for engagement in core banking businesses and dearth of funds to pay their staff strengths, leading to retrenchment of their staffs and adding more unemployment into the already clustered Nigerian unemployed workforce.

The impact of the oil price fall spills over to the banks in such a fluid manner, because activities in the oil sector are financed by the banks and a well-developed banking sector contributes to economic growth by mobilizing savings and efficiently allocating them among the competing investment projects and other demands for funds (Chris and Onyinye, 2015). The falling oil prices cause serious financial problem for the oil sector and the capital market due to their link to the financial world and the Nigerian banks. Since, banks sit at a vantage position in the economy, failure to repay the loans advanced to the oil marketers left a bad effect on the banks' balance sheet, and such loans became bad loans, which is a strain on banks' capital adequacy. Hence, the oil price fall calls for several regulatory measures to be adopted to cushion the effect on the economy because, only a sustained and stable macroeconomic environment and a sound and vibrant financial system can propel the economy to achieve our national desire to become one of the 20 largest economies in the world by the year 2020 (Soludo 2007).

Therefore, to curb the effect of the bad loan debts on the loan profile of some affected banks, the CBN through a circular directed all banks to restrict loan defaulters from further assess to loan facilities, some of the loan defaulters were oil marketers. The CBN also engaged them in a rigorous manner to recover the money, such as through a circular directive to the banks, dated April 22 2015, that the names of those who defaulted for a period of at least one year on the servicing of their loans facilities be published on three national dailies and shaming them, and that the exercise to be done every three months. The circular directive also banned them from participating in Nigerian foreign exchange market. Although, it is a well calculated effort to recover loan debts and keep the affected banks in shape, however, care needs to be taken so that it does not erode confidence and confidentiality trust of investors who wants to borrow from Nigerian banks. The affected banks also sanctioned themselves and their erring staffs, who signed off on the loans and some of the banks stopped advancing loans to the energy sector.

Furthermore, Patti and Ratti, (2015) noted that, oil price increase has a greater influence in the economy compared to an oil price decrease. Korhonen and Juurikkala (2013) argued that when oil price appreciates, there is a real exchange rate appreciation in oil exporting countries; this is because, they earn a significant amount of money from oil exportation. Therefore, when the oil price falls, oil dependent nation suffers exchange rate depreciation. Nigeria is renowned as being one of the major oil importer and exporter and it is experiencing oil price decrease. Flowing from this, it will be logical to state that when the price of oil falls, the exchange rate inNigeria will depreciate. This translates to the depreciation of the Nigerian currency, the Naira as it goes to a steady decline. As at the 16th February 2016, the Naira had declined to ₦345 to the Dollars in the parallel market. Although, it has been alleged that the sharp decline is due to the huge demand for the dollars, with no commensurate supply of the commodity. This made the few Bureau d Change operators to sell Dollars at astronomical prices. This could be a factor; however, dominant as a prevailing factor, is the fact that the oil price has fallen and has hit the Nigerian capital market.

The need for diversification of the Nigerian economy

Although, the oil price fall crisis may not persist always, however, since the Nigerian economy is renowned to be oil dependent, there is a need to look inwards for a re alignment of priorities for the economy to be viable, and forestall any present or future oil price fall crisis on the economy, thus a call for a shift from the oil sector into areas that were neglected or not paid rapt attention. The cry for diversification of the Nigerian economy has been long overdue and overwhelming. Considering the harsh economic realities the falling oil price had shown on the economy, the have been series of renewed calls for the diversification of the Nigerian economy by various individuals.This is because of the prevailing urgency of the effect of oil price fall on the Nigerian economy, which is frying the Nigerian economy.

Diversification is seen as a panacea for stabilizing the Nigeria financial economy and taking it away from oil price fall implications. This is because, in other climes battling with oil price fall, the impact is not severe, due to the non-reliance on the oil sector. Focus and energy was dedicated to other non-oil sectors, for example, China and South Korea are known for manufacturing of commodities, India is known for Information technology infrastructures; these countries' economies are sustained and blooming in this oil price fall era.

The Nigerian financial environment is not left out, as they were calls on the need for diversification of their lending portfolio and re focus of their lending priorities to other areas and sectors of the economy. For example, in the area of Small and Medium Scale Enterprises (SME)'s, Duru and Kehinde (2015) had argued that 'Small and Medium Scale Enterprises' (SME)'s play important roles in the process of industrialization and economic growth, apart from increasing the per capita income and output, SME's create employment opportunities; enhance regional/ sectoral economic balance through industrial dispersal and the promotion of resource utilization.' To inspire this idea, the CBN directed Nigerian banks to diversify and increase their lending portfolio to other sectors of the economy in ways that would re jig the production wheel and fuel economic activities in the country. In December 2015, 7 the CBN governor had lamented on the less attention paid to the SME's sector. He noted that less than 50 percent of the ₦220 billion of the Micro Small and Medium Scale Enterprises (MSME)'s loan has been assessed since its creation in 2012, despite the sum of ₦40.3 billion been disbursed to state government, commercial banks, microfinance banks and financial cooperatives. Also, to support lending to the SME's, in December 2015, the CBN Governor and commercial banks under the aegis of the banker's committee, at a two days seventh banker's committee retreat in Lagos, Nigeria, titled; creating an enabling environment for SME's growth, had mandated commercial banks to lower their risk rating for SMEs or lose their cash reserves ratio (CRR). The cash reserve ratio (CRR) is a portion of the banks 'deposit kept with the CBN as reserves.

Oil and the Nigerian Economy

Prior to the discovery of crude oil in commercial quantity in 1956 (Adedipe, 2004; Odularu, 2007), the Nigerian economy, though largely agrarian (Canagarajah and Thomas, 2001), was stable and steadily growing. The pleasant situation continued into the 1960s when agriculture played a dominant role in her economy in terms of contribution to GDP and foreign exchange earnings (Kwanashie, Ajilima and Garba, 1998). The stability and gradual growth of the economy reversed in the era of oil-dominant economy. The reversed situation was synonymous with decline in the roles played by agriculture.

The sector shrank in GDP contribution from 66% in 1958/59 (Kwanashie, Ajilima and Garba, 1998) to 16% in 2004 (United State Agency for International Development, 2006). Its contribution to the nation's export revenues and foreign exchange earnings plummeted from 86% in 1955-59 (Aigbokan, 2001) to 1.8% in 1996 (Balogun, 2001). These worrisome declines have been attributed to growing activities of oil and mining industy in the country (Kwanashie, Ajilima and Garba, 1998).

Balogun (2001) attributes this problem to the poor management of public resources and inappropriate incentives, which in turn may not be unconnected with overwhelming inflow of oil revenues in the 1970s. Crude oil has metaphorically been referred to as the 'black gold' Bamisaye and Obiyan, 2006). The resource has redefined the global economy in general and the Nigerian economy in particular. The impact of crude oil on Nigerian economy has been double-edged. It has benefited the country in some ways, and has in many other ways turned out to be a curse (Ogwumike and Ogunleye, 2008). Crude oil's contribution to GDP rose from 1.6% in 1960 to 11% in 2001 (Adenikinju, 2006).

This contribution consists of proceed from oil export, local sale of crude oil for domestic refining and local sale of natural gas. However, the contribution has been limited due to substantial involvement of foreign investors in the oil sector, and consequent repatriation of the sector's profits and dividends abroad (Odularu, 2007). Crude oil also contributes over 90% of foreign exchange earnings in Nigeria (Adedipe, 2004; Adenikinju, 2006). Ogwumike and Ogunleye (2008) concur that the sector dominates other sectors in contributing to export revenues. For instance, it was responsible for over 98% of total export from the country in 2005. Moreover, the sector contributes to provision of employment in the country (Odularu, 2007). The contribution has however not been relatively significant because it has limited linkages with the rest of the economy (Ibrahim, 2007). As a result, the sector employs only 1.3% of the total modern sector employment in Nigeria (Odularu, 2007). This is due to setbacks caused by oil-related activities.

Methodology

The study focuses on finding out the impact of dwindling oil prices in the Nigeria economy. The population of the study comprises of Nigeria economy institution which includes, regulatory and operating institution. Operating institution in the Nigeria economy include gross domestic product (GDP) as a measure of national productivity and crude oil, industrial/services products, and capacity utilization. The method of data collection to be used is mainly secondary. This is informed by the nature of the study being mainly explanatory. For the purpose of this research, the data for this study was obtained mainly from secondary sources particularly from the Federal Office of Statistics (FOS), Central Bank of Nigeria (CBN) research and development department, Nigerian Stock Exchange (NSE) Fact books, Security and Exchange Commission (SEC) market Bulletins. However, the bulk of the information used was gotten from the Central Bank of Nigeria (CBN) statistical bulletin (2007-2016).This study adopts descriptive statics such as mean and standard deviation and inferential statistics which include Regression and Correlation analysis.

Model specification

Operational variables used in this study are gross domestic product (GDP) as a measure of national productivity and crude oil, industrial/services products, and capacity utilization. The model is developed as:

GDP = f (COP, AGP, ISP, CUZ, VTR) where

GDP = Gross Domestic Product.

COP = Crude Oil production.

ISP = Industrial/Services Production.

CUZ = Capacity utilization.

VTR = Value Traded Ratio

Result and Discussion

Decision Criteria:

Findings based on the use of correlation shall adjudge significance at 5% level of significance where about correlation is ≥ 50%. Where P-test is ≤ 0.05 and T-test± 1.96.

Relationship between Dwindling Oil Price and Nigeria Economic.

Preamble

The empirical analysis of the activities and performance of Nigerian economy within a period of ten years (2007-2016) was presented in this section. Data obtained from secondary sources were analyzed in relation to the various objective of the study. This part of the study is divided into two; the first part gives the descriptive analysis while the second part gives the inferential statistical analysis of the data.

Descriptive Statistics of the variables

Presented in the table below is the descriptive statistics of the variables. The result shows that Gross Domestic Product (GDP) has a mean value of (N716.009billion), maximum and minimum value of (N950.11billion) and (N527.58billion) respectively. The standard deviation of (143.1997) shows there is significant deviation from the mean. Crude Oil Production (COP) has a mean value of (1233.737), maximum value of (2078.31) and minimum value of (400.41). The standard deviation of (578.56) shows a significant dispersion from the mean. Industrial Service Production (ISP) has a maximum value of (249798.2) and a minimum of (42802.99). The standard deviation of (76139.38) shows a significant dispersion from the mean value (120143.5). Capacity Utilization (CUZ) has maximum and minimum values of (57990.2) and (20730.6) respectively with a mean value of (30629.69). The standard deviation of (11518.5) shows a significant deviation from the mean. Value Traded Ratio (VTR) variable has mean value of (206.3), a maximum value of (215) and a minimum value of (192). The standard deviation of (8.628763) shows significant dispersion from the mean.

Descriptive Analysis of Variables showing the relationship between Dwindling Oil Price and Nigeria Economic.

Variable	Observation	Mean	Standard Deviation	Minimum	Maximum
Year	10	2008.5	3.02765	2004	2013
GDP	10	716.009	143.1997	527.58	950.11

COP	10	1233.737	578.5552	400.41	2078.31
ISP	10	120143.5	76139.38	42802.99	249798.2
CUZ	10	30629.69	11518.5	20730.6	57990.2
VTR	10	206.3	8.628763	192	215

Source: Researcher's Computation, 2017.

Regression Analysis of the relationship between Dwindling Oil Price and Nigeria Economic.

A multiple regression analysis whose equation is presented below found that the coefficient of determination (R-square) is 0.9132. This shows that the predictive power of the independent variable (Dwindling Oil Price variables) as used to explain variation in the dependent variable (Nigeria Economic proxied by GDP) is about 91% with a high adjusted R-square of (0.8438). The combined P value of 0.0073 and F-Value of 60.43 shows there is a significant relationship and effect between the variables examined. The regression equation is as shown below.

GDP=1468.087+0.2810COP+0.00059ISP-0.0104CUZ-3.8632VTR

The result shows that COP shows a positive contribution of 28%, COP had a marginal positive contribution of about 0.059% to the variation in GDP. CUZ indicated a negative but marginal contribution of 1.04% to changes in GDP while VTR showed a negative contribution of about 3.863 to changes in GDP. The regression table is as shown below:

Results of the Regression Analysis Showing the Relationship Dwindling Oil Price and Nigeria Economic.

Dependent variables	**Independent variables**	**Coefficient**	**Standard Error**	**T**	**p>|t|**	**[95% conf. interval]**
GDP	**COP**	.2899558	.0689144	4.21	0.008	.1128057 .467106
	VTR	.0000599	.0003994	0.15	0.887	-.0009667 .0010865
	CUZ	-.0104484	.0025184	-4.15	0.009	-.0169223 - .0039746
	VTR	-.863164	2.643678	-1.46	0.204	-10.65895

						2.932626
	constant	1468.087	551.2917	2.66	0.045	50.94668 2885.228
R-squared =0.9132	**Adj. R-squared = 0.8438**		**P≤0.05**		**F (4,5)= 60.43**	

Source: Researcher's Computation, 2017.

A pairwise correlation test between the variables indicates similar result given correlation between GDP and other explanatory variables. The coefficient of correlation (R) between COP and GDP is (0.6604), an indication of significant and positive relationship. ISP has a moderate positive correlation of (0.4038) with GDP and the variable CUZ has a weak correlation coefficient of (0.0148) with GDP. VTR shows a negative but moderate correlation coefficient of (0.5974) with GDP.

Result of pairwise correlation between Dwindling Oil Price and Nigeria Economic.

	GDP	**COP**	**ISP**	**CUZ**	**VTR**
GDP	1.0000				
COP	0.6604*	1.0000			
ISP	0.4038	0.7389*	1.0000		
CUZ	0.0148	0.7184*	0.5791	1.0000	
VTR	-0.5974	-0.2973	0.0301	0.0207	1.0000

Source: Auditor's Computation, 2017

Test of Hypothesis:

Decision criteria: If Fcalc > Ftab; reject Null hypothesis and accept alternative hypothesis.

If Fcalc < Ftab; accept Null hypothesis and reject alternative hypothesis.

Hypothesis:

H_0: There is no significant relationship between dwindling oil prices and the Nigeria economy

H_1: There is significant relationship between dwindling oil prices and the Nigeria economy

Decision criteria:

With a calculated F-value of 60.43 as compared with a tabulated F-value of 5.19 (at 5% level of significance), the null hypothesis is rejected while the alternative hypothesis is accepted, with the conclusion that there is significant relationship between dwindling oil prices and the Nigeria economy.

Conclusion

This study examined the activities and performance of dwindling oil price. With respect to the objectives of the study, the following conclusions were reached;

i. Dwindling oil price indicators significantly influence Nigeria Economic Development within the study period.

ii. Dwindling oil price and Nigeria economy exhibit significant relationship within the study period.

This conclusion is consistent with results reported by (Ogundipe, Oluwatomisin et al, 20114)

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