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THE IMPACT OF OIL PRICE ON THE NIGERIAN ECONOMY

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Abstract
This study contends that upward adjustments of petroleum productsprices have resulted in inflation, high cost of living, and inequitable distribution of income in Nigeria. Between 1978 and 2007, the various Nigerian regimes increased fuel prices a total of 18 times. Most of the increase occurred in the 1990-2007 period when prices were adjusted, sometimes twice a year. The objectives of the study were to examine the economic impacts of price instability and identifying the causes of increase in prices of oil products.. The assumptions of the study are that the rise in price of petroleum products has contributed significantly to inflation in Nigeria, using simple regression analysis of data to find out the relationship between dependent and independent variables. The study revealed that whenever petroleum increases, the inflation rate also increases. The explanation for the above result is that the relationship between the inflation rate and the price of petrol is significant. The study recommended that more resources should be tapped to diversify the economy.

Keywords: Oil, price, inflation, increase

Introduction

Oil products are derived from crude oil and they include petrol, diesel, kerosene, natural gas, bitumen.. Oil was discovered in Nigeria in 1956 at Oloibiri in the present Bayelsa State, after a century of searching (Dharam,1991).

Oil products are basically used in industries for production of goods and services and they are also used domestically for personal consumption in which the greater percentage of it comes from developing countries. The oil industry is very important to the Nigerian economy. It provides among other things the greatest part of the foreign exchange earnings and total revenue needed for socio-economic and political development of Nigeria.

The bulk of Nigerian crude oil is sold unrefined and when refined, the products range from petrol to heavy liquids for road tarring.

Government has been the custodian of petroleum and its products in Nigeria. Though, this brought a temporary growth in the economy, the price instability of the crude oil in the world market has led to the downfall of Nigerians economy in various sectors, such as the production, manufacturing and services sectors.

Statement of the problem

The upward adjustments of petroleum products have resulted in inflation, high cost of living, inequitable distribution of income in Nigeria. Between 1978 and 2007, the various Nigerian regimes increased fuel prices a total number of 18 times. Most of the increase occurred in the 1990-2007 period when petroleum products prices were adjusted upwards sometimes twice in one year. One major problem this has caused was the instability of the prices of goods and services in the country. Whenever there is an increase in prices of oil products, it affects transportation, cost of good and other services.

Research questions

The questions to be answered in this paper are as follows:

1. How adverse is the price instability of oil products on Nigeria economy?
2. Is the discovery of crude oil the cause of neglect of other sectors of the economy?
3. Is Nigeria poor because of oil?

Theoritical framework

Etiebet (1999) observed that price of oil products is derived from crude oil prices and it therefore follows that prices of petroleum products should trail crude oil prices. According to the author, it is not always the case for a number of reasons. In the first place, there is always a time lag between crude oil processing and product distribution through network.

Secondly, for socio-political reasons, government of both oil producing and consuming countries should invariably intervene in the market to influence products price determination. But in the actual fact, the extent of intervention depends on the specific needs of the country and the level of endowment of the products in question. The author noted that trailing oil products prices down crude oil prices has revealed that, crude oil cost is not the only cost incurred in supply and distribution of petroleum products. Other costs include refining, storing, transporting and distributing, the author asserted.

Siddy (1999) asserted that the causes of price instability is attributed to scarcity caused by refinery maintenance and rehabilitation problem, low capacity utilization, supply, and demand inequality. The political change that Nigeria went through, which turned over the administration and endured a lingering economic down turn is enough reason to cause price instability of oil products in Nigeria. The author opined that trailing oil products prices down to crude oil prices has revealed that the instability in the prices of oil products was due to cost of refining, storing, transporting distributing and inefficiencies in the process.

Dan (1999) asserted that Nigeria has four refineries, one of which is at Kaduna, Warri and two at Port-Harcourt with a total nominal refining capacity of 445,000 barrels per day. The author noted that although the refineries find it very difficult to reach that (445,000) due to frequent breakdown and operating problems such as vandalisation, which has been reduced and that more products are being pumped throughout the pipelines.

Mbendi (2000) argued that in theory, Nigeria's refineries capacity is sufficient to meet its domestic consumption requirement. In practice, however, according to the author, the country has experienced frequent shortage of refined products since it refineries have poor configuration and operation inefficiency. The author stated that it has been estimated that smuggling amounts to over 320,000 barrels per day largely to Benin Republic, Niger, Chad, and Cameroon. The author noted that Nigeria has become a large importer of light petroleum products, importing thousands of tons of refined products.

Runl (2010) asserted that people say Nigeria is dominated by oil and they are right because Nigeria seems to be exporting noting but oil. The government revenues are so dependent on oil, which has been managed quite protectively. But it's still extremely undesirable that internally generated revenue are such a small part of Nigeria's revenue because essentially, it means that all the revenues of the government is just coming down from heaven. It's like a gift and it is easy to waste a gift. The author noted that Nigeria is poor because of oil.

Ewa and Agu (2003) shared their view that the dominance of petroleum in Nigerian economy has led to instability in the economy, which as a result makes price instability of oil products to be more prevalent in Nigeria than other countries.

The author observed that smuggling is attractive and profitable due to price differential. This act of smuggling oil products from Nigeria to her neighbouring countries is one of the factors which made price instability of oil products to be prevalent in Nigeria.

In summary, the works reviewed are the work of many individuals who have shown concern in the area of this study. The most reoccurring term in the works reviewed were that price instability of oil products are prevalent due to ill-refinery maintenance, and rehabilitation problems, low capacity utilization, supply and demand inequality reduction in crude oil allocation, and smuggling of petroleum products.

The hypothesis of this study is that, the rise in price of petroleum products has not contributed significantly to inflation in Nigeria.

Methodology

Materials and information were obtained from the CBN Annual Report and statement of Account, CBN Financial review, IMF consultancy Report, The World Fact Book, Books and Annual Reports of private petroleum producing Companies.

The method that was used in analyzing the data is simple regression analysis. The price of petrol is the variable (X) while the inflation rate is variable (y).

Table 1

Year	Petroleum, price per litre	Inflation rate
1991	0.7	12,695
1992	3.25	44.808
1993	11	57.165
1994	11	57.032
1995	11	72.852
1996	11	29.262
1997	11	8.536
1998	11	9.986
1999	20	6.611
2000	22	6.938

2001	26	18.032
2002	30	13.081
2003	40	14.023
2004	55	15.02
2005	60	17.856
2006	65	8.227
2007	70	5.392
2008	65	11.583
2009	65	11.959
2010	65	11.50

Sources: Olorunfemi S, Natural gas option in Nigeria and International Monetary Fund World Economic outlook, 2010.

Discussion of the findings

From the analysis, the co-efficient of regression, i.e. b is positive (b = 34.47). This simply shows that the two variables X and Y tend to change (increased) in the same direction. In other words, whenever the price of petroleum increases, the inflation rate also increases. The explanation for the above result is that the relationship between the inflation rate and the price of petrol is significant.

Hence, we reject the null hypothesis which says; the rise in price of petroleum product has not contributed significantly to inflation in Nigeria. This shows that an increase in petroleum price will also lead to an increase in the inflation rate in Nigeria.

The pricing of oil products has always been controlled by the government at all level in the industry, depending on the international price of crude oil which is set by the Organisation of Petroleum Export Countries (OPEC). This means that domestic prices of oil products are based on international prices of crude oil. The government regulates the transfer prices paid within NNPC and sets product prices at wholesale and retail levels.

The NNPC subsidiary Pipelines and Product Marketing Company (PPMC) buys crude oil at prices set by the government; they refine and then sell the refined products to the marketing companies. Retail prices are subsidized by the government and the subside could be high or low depending on the international price of oil which is set by Organisation of Petroleum Exporting Countries (OPEC). It was estimated that the government pays an amount of $2.5 billion U.S. dollars as subsidies, consequently resulting into price instability of oil products.

Another cause of price instability of oil products in Nigeria are attributed to widespread smuggling and diversion of products from their approved destinations, holding of products in anticipation of an increase in prices and the refineries producing at less than half of their installed capacities.

The rapid growth of population in this country is an enough reason to cause instability in prices of oil products, because the higher the population of Nigeria with low capita income, the higher the unskilled labour and high rate of unemployment.

All these are the ripple effect of price instability as a result of inflation. We can conclude that because of predominant position of oil products on the Nigerian economy, anything that affects it such as the instability in the prices of oil products will affect the economy as whole.

Recommendations

Having established that price instability affects Nigerian economy as a whole, the paper recommends the following solutions:

1. Due to the heavy reliance or dependence on the petroleum products, the government should strive to make the products available at all time.
2. More of other resources should be tapped so as to diversify the economy.
3. The distribution channel of the flow of the petroleum products should be well monitored to avoid disruption of distribution or scarcity.

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