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Premium Motor Spirit Subsidy Removal and Implications on Business and Economy in Nigeria

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Impact of Insurance Sector Development on the Growth of the Nigerian Economy

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Abstract
The removal of premium motor spirit subsidies represents a pivotal policy decision in many developing economies, including Nigeria. This paper examined the multifaceted implications of fuel subsidy removal on businesses of varying scales – large, medium, and small – and the subsequent impact on overall economic growth in Nigeria. The research sheds light on the intricate dynamics that unfold when fuel subsidies are eliminated. The study employed a qualitative approach to explore literature on the subject matter. Findings indicate that while the removal of fuel subsidies initially results in increased fuel prices, which impact transportation costs and the prices of goods and services, the implications on businesses vary significantly based on their size and sector. Large corporations, with greater capacity to absorb cost increases, often experience minimal disruptions and may even benefit from reduced competition. Medium-sized businesses face a more nuanced situation, as they navigate increased operational costs while striving to maintain market share. Small-scale enterprises are particularly vulnerable, as higher costs can lead to reduced profitability and potentially force some to cease operations. The study also identifies potential positive outcomes. The redirection of government resources from subsidies to critical sectors, such as infrastructure and education, can stimulate economic diversification and long-term growth. Moreover, the removal of subsidies can incentivize energy efficiency, innovation, and investment in alternative energy sources, fostering sustainable development. The paper contributed valuable insights into the implications of fuel subsidy removal on businesses of different scales and its wider impact on economic growth in Nigeria. The findings underscore the importance of targeted policies that cushion the immediate impact on vulnerable businesses, foster economic diversification, and promote sustainable growth. By understanding and addressing the diverse challenges and opportunities that arise from subsidy removal, policymakers can navigate this complex transition while fostering a more resilient and prosperous economy.

Keywords: Fuel Subsidy Removal, Businesses, Economy, Economic Diversification, Social Impacts

Introduction

Premium motor spirit subsidies, otherwise referred to as fuel subsidies in a developing country like Nigeria have a long history and have played a significant role in the country's economy. Nigeria, as a major oil-producing country, has historically provided fuel subsidies to its citizens due to the perception that it is an equitable way of sharing the country's oil wealth (Alemika & Aiyede, 2012). The Nigerian government implementation of fuel subsidies policy is a means to ensure affordable and stable fuel prices for its citizens. Fuel subsidies is one of government interventions to keep fuel prices artificially low by providing financial support to fuel importers and distributors (National Bureau of Statistics, 2021). The significance of fuel

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subsidies lies in their impact on various aspects of the Nigerian economy, including businesses, government finances, and social welfare programs. Basically, subsidies involve the government providing financial support to reduce the cost of fuel for consumers. So, fuel subsidies have been a prominent feature of Nigeria's economic landscape for several decades. The singular aim of fuel subsidies policy implementation by the government is to reduce the cost of petroleum products for consumers and businesses, making them more affordable and supporting economic development. However, the efficacy and sustainability of fuel subsidies have been subject to debate and scrutiny in recent years.

The genesis of fuel subsidies in Nigeria can be traced back to the 1970s, a period of oil boom when the government sought to alleviate the burden of rising fuel prices on the populace (Olomola, 2012). In the view of Eze et al. (2018), fuel subsidies in Nigeria can be traced back to the 1970s when the government came up with measures to ensure the availability of affordable fuel for its citizens. The first fuel subsidies in Nigeria were introduced in the 1970s as a response to the oil price shock. The government at the time feared that the high price of fuel would lead to widespread unrest, so it decided to provide subsidies to keep the price of fuel low. Over time, the subsidy regime expanded, leading to significant fiscal implications for the government. The primary objective was to mitigate the effects of rising international oil prices on domestic consumers. Over time, however, the subsidy program became increasingly burdensome for the government due to the high costs associated with maintaining artificially low fuel prices (Iwayemi et al., 2019). This influenced the need for fuel subsidy removal by the Federal government in Nigeria.

The issue of fuel subsidy removal in Nigeria has been a contentious and complex subject, deeply intertwined with the country's economic, social, and political landscape. However, the removal of these subsidies has been a recurring theme in Nigeria's economic reform discussions, driven by factors such as fiscal sustainability, global oil price fluctuations, and the need to redirect resources towards other developmental priorities. As Nigeria's population grew and demand for fuel increased, the cost of fuel subsidies began to strain the government's finances. The subsidies created a situation where the government was spending substantial amounts to keep fuel prices low, resulting in fiscal imbalances and diverting resources from critical sectors such as healthcare, education, and infrastructure. The global oil market's volatility also played a pivotal role in the discussions surrounding fuel subsidy removal in Nigeria. The country's heavy reliance on oil exports meant that fluctuations in global oil prices directly impacted its revenue. When oil prices are high, the burden of fuel subsidies is somewhat manageable, but during periods of low oil prices, the subsidies become an unsustainable financial liability.

The need for economic diversification and structural reforms became increasingly evident as Nigeria faced the challenges posed by its oil-dependent economy. Advocates for subsidy removal like Adenikinju, Ebohon (2012); Akpan and Atan (2019); Falola and Heaton (2008); Oyedemi (2016); Umoru and Adeniy (2020) argued that it was essential to reduce the government's fiscal vulnerability to oil price fluctuations. They also stressed the importance of redirecting resources towards sectors that could drive sustainable economic growth and reduce the country's dependence on oil revenue. Several Nigerian governments attempted to address the issue of fuel subsidy removal, but each effort was met with significant public backlash (Umoru & Adeniy, 2020). The subsidies have become deeply ingrained in the daily lives of citizens, and any attempt to remove them have been met with protests and opposition. This highlighted the challenge of balancing economic reforms with the social implications of removing a subsidy that many Nigerians relied on (Umoru & Adeniy, 2020).

Implications of Premium Motor Spirit Subsidy in Nigeria

Fuel subsidies have held significant economic and political importance in Nigeria. Economically, they have provided a measure of stability and affordability in fuel prices, benefiting consumers and businesses alike. By reducing the cost of transportation and production, fuel subsidies facilitated economic activities and contribute to business growth (Adesoye et al., 2018). Moreover, fuel subsidies have been seen as a social welfare measure, intended to alleviate poverty and mitigate the impact of high fuel prices on the most vulnerable segments of society (Iledare et al., 2019). The implication of fuel subsidies in Nigeria extends beyond economic considerations. Politically, fuel subsidies have been used as a means of political patronage, with successive governments using them as tools for social and political stability (Eromosele & Ezeoha, 2017). This has resulted in a complex interplay between economic interests, social welfare objectives, and political considerations, making fuel subsidies a highly contentious issue in the country.

The imperativeness of fuel subsidies in Nigeria stems from several factors which include affordability of fuel, political and social stability, favourable influence on the economy and removal of fiscal challenges. Fuel subsidies have aimed to make fuel more affordable for Nigerian consumers, particularly low-income households who heavily rely on fuel for transportation and electricity generation (Iwayemi et al., 2019).

The availability of subsidized fuel has been seen as a means to maintain social and political stability by ensuring access to basic commodities and preventing public discontent over high fuel prices (Falola et al., 2020).

Fuel subsidies have had implications for business operations and economic growth. By keeping fuel prices low, subsidies have helped businesses in sectors such as transportation, manufacturing, and agriculture manage their operating costs (Falola et al., 2020). The government's fiscal capacity has been strained by the substantial financial resources required to sustain fuel subsidies (Okon & Adedeji, 2017). The costs of fuel subsidies have contributed to budget deficits, hindered public investments in infrastructure and social programs, and increased public debt (Iwayemi et al., 2019). A key significant effects of fuel subsidies on the Nigerian economy is that they distort the market for fuel (World Bank, 2018). The artificially low price of fuel encourages consumers to use more fuel than they would if the price were higher. This leads to increased demand for fuel, which can put upward pressure on prices. Fuel subsidies also have a significant impact on the government's budget. The government spends billions of dollars each year on fuel subsidies (Adenikinju, 2013). This money could be used for other purposes, such as education or healthcare.

Assessment of Implications of Premium Motor Spirit Subsidy Removal in Nigeria

The removal of fuel subsidy by the government of Nigeria no doubt has myriad impacts/implications Some of these encompass economic impact, social impact, impact on government finances, economic diversification implication, inducing foreign exchange pressure, environmental impact, political consideration, energy sector reforms and long-term benefits respectively. Economic impact of fuel subsidy removal mainly encompasses inflationary impact, high cost of living, and production costs. Removing fuel subsidies often leads to an immediate increase in fuel prices. This can have a cascading effect on transportation costs and the prices of goods and services throughout the economy, contributing to inflation. Higher fuel prices directly impact household budgets, especially for lower-income groups. The increased cost of transportation and goods can erode purchasing power and reduce the standard of living for many Nigerians. Industries that rely heavily on transportation, such as agriculture and manufacturing, could experience higher production costs. These additional costs may be passed on to consumers, further driving up prices.

The social impacts of fuel subsidy removal include public protests, and social inequality. Historically, fuel subsidy removal has triggered protests and social unrest due to the immediate impact on citizens' lives. Protests can disrupt economic activities and challenge political stability. The removal of fuel subsidies can disproportionately affect low-income and vulnerable populations, exacerbating income inequality and social disparities. Fuel subsidy removal impacts on government finances; has implications on economic diversification and induce foreign exchange pressure. Eliminating fuel subsidies releases funds that can be redirected to other sectors such as education, healthcare, and infrastructure. However, effective budget reallocation requires transparent and accountable governance to ensure that these funds are optimally utilized. The removal of fuel subsidies could nudge the government and private sector to invest more in non-oil sectors, helping to diversify the economy and reduce dependence on oil revenue. Nigeria imports a significant portion of its refined petroleum products. Higher fuel prices increase import costs, which could contribute to foreign exchange pressure and a weaker local currency.

Similarly, premium motor spirit subsidy removal commands negative environmental political impacts. Higher fuel prices can incentivize consumers to use fuel more efficiently and consider alternative energy sources, which could have positive environmental implications. The government's handling of fuel subsidy removal can impact its popularity and legitimacy. Public opposition may influence political decisions. Removing fuel subsidies can signal the government's commitment to fiscal discipline and economic reform, potentially boosting investor confidence in the long-term stability of the economy. The removal of subsidies could encourage investments in domestic refining capacity, reducing Nigeria's reliance on imported refined products. Over the long term, removing fuel subsidies can contribute to a more sustainable economic growth trajectory by allowing the government to invest in critical sectors, infrastructure, and human capital development.

Implications of Premium Motor Spirit Subsidy Removal on Businesses and Economic Growth in Nigeria

Premium motor spirit subsidy removal in Nigeria has distinct implications for businesses of different sizes, ranging from large corporations to medium-sized enterprises and small businesses (Amponsah, Asenso, & Oteng-Abayie, 2020). Large businesses often have more resources and operational flexibility, which can help them navigate the effects of fuel subsidy removal (Amponsah, et al. 2020). Large businesses with extensive operations and supply chains will experience increased transportation costs due to higher fuel prices, potentially impacting their profit margins (Jones, 2018). Increased transportation costs can disrupt supply chains, affecting the timely delivery of raw materials and finished goods (Amponsah et al., 2020). These businesses may have the capacity to diversify their energy sources, investing in alternative energy solutions to mitigate the impact of higher fuel costs (Ahiakpor, 2019).

Medium-sized businesses often operate with tighter budgets and limited resources, making the implications of fuel subsidy removal particularly pronounced. Medium-sized businesses may struggle to absorb the additional fuel costs, leading to decreased profit margins (Okafor, 2016). Higher operational costs can make it challenging for medium-sized enterprises to compete with larger competitors that have more resources to manage cost increases (Okoh & Okolie, 2017). Small businesses, being the most vulnerable, can face severe challenges due to fuel subsidy removal. Small businesses often operate on thin profit margins and limited resources. The sudden increase in fuel costs can threaten their survival and viability (Aremu & Adeyemi, 2017). As consumers cut back on spending due to rising prices, small businesses may experience reduced demand for their products and services (Omodero & Ezeaku, 2019). Small businesses might lack the financial capacity to invest in alternative energy sources or adapt their operations, making them more susceptible to the impact of fuel price hikes (Anyanwu et al., 2021).

Fuel subsidy removal has been a topic of intense debate in Nigeria due to its potential impact on economic growth. While the intention behind subsidy removal is often to improve fiscal sustainability and promote long-term economic development, the immediate effects can be complex and multifaceted. Fuel subsidy removal can contribute to inflationary pressures in the economy. When subsidies are removed, fuel prices tend to rise, leading to increased transportation costs and higher prices of goods and services. This phenomenon has been observed in previous instances of subsidy removal in Nigeria (Adenikinju & Ebohon, 2012). Higher fuel prices resulting from subsidy removal can lead to reduced disposable income for consumers, impacting their purchasing power. This, in turn, can lead to decreased consumer spending, potentially affecting demand for goods and services and thereby slowing economic growth (Akpan & Atan, 2019).

Industries that rely heavily on transportation and energy, such as manufacturing and agriculture, may experience higher production costs due to increased fuel expenses. These increased costs could reduce the competitiveness of Nigerian products both domestically and internationally, potentially affecting economic growth (Oyedemi, 2016). While subsidy removal can increase government revenue by reducing the need for fuel subsidy expenditures, the impact on overall government expenditure is crucial. Proper allocation of the saved funds towards productive sectors like infrastructure, education, and healthcare is essential to support economic growth (Umoru & Adeniyi, 2020). The removal of fuel subsidies can signal the government's commitment to fiscal discipline and economic reforms. This could boost investor confidence, attracting foreign direct investment (FDI) and domestic investment that can contribute to economic growth (Akpan & Atan, 2019). Subsidy removal can serve as a catalyst for broader structural reforms and economic diversification efforts. The need to reduce dependence on oil revenue and encourage investments in non-oil sectors becomes more pressing, potentially leading to more sustainable economic growth in the long run (Akpan & Atan, 2019).

Theoretical Framework

This paper is hinged on the crowding out theory, resource recourse theory, supply and demand theory, fiscal policy and crowding out theory, and structural transformation theory. The crowding out theory suggests that when government expenditures increase, particularly in response to the removal of subsidies, it can lead to a reduction in private sector spending and investment. In the context of fuel subsidy removal in Nigeria, the government might redirect the funds saved from subsidies to other sectors such as healthcare, education, and infrastructure. While these investments can have positive long-term effects on economic growth, the immediate increase in government spending could compete for resources with private sector investment, potentially crowding out private initiatives and dampening economic growth (Friedman, 1956). This theory underscores the importance of effective resource allocation by the government and the need to balance public and private sector interests to ensure sustained economic growth.

The resource curse theory posits that countries heavily dependent on a single natural resource, such as oil, can face negative economic consequences due to factors like volatile commodity prices, corruption, and a lack of economic diversification (Auty, 1993). In Nigeria's case, the removal of fuel subsidies could be viewed as an attempt to reduce dependence on oil revenue. By reallocating funds to non-oil sectors, the government aims to diversify the economy and mitigate the adverse effects of oil price fluctuations.

However, if the transition away from oil is not managed effectively, it could lead to challenges in absorbing the displaced labor force, low productivity in new sectors, and difficulties in attracting investment. Thus, while fuel subsidy removal aligns with the goal of economic diversification, its success hinges on comprehensive strategies that ensure sustainable growth in non-oil sectors. The supply and demand theory suggests that the removal of fuel subsidies can lead to an increase in fuel prices due to reduced supply (as subsidies are removed) and unchanged or even increased demand. This price increase can have a cascading effect on the cost of production and transportation, leading to higher prices for goods and services across the economy. As a result, consumer purchasing power may decrease, potentially leading to reduced aggregate demand and economic growth (Mankiw, 2014).

According to the fiscal policy and crowding-out theory, the removal of fuel subsidies can free up government resources. While this could potentially allow for increased public investments in sectors like infrastructure and education, if not managed properly, it might also lead to increased government borrowing from the private sector. This could crowd out private investment, potentially limiting economic growth (Barro, 1990). The structural transformation theory posits that removing fuel subsidies can be a part of broader structural reforms aimed at diversifying the economy away from dependency on oil. By reallocating resources from subsidies to strategic sectors like agriculture, manufacturing, and technology, Nigeria can stimulate growth in non-oil sectors, reducing vulnerability to oil price fluctuations (Rodrik, 2013).

Empirical Review

Several studies have been conducted to ascertain the implications of premium motor spirit (PMS), otherwise known as fuel on large, medium, small -scale businesses and the economy of a developing country like Nigeria. For instance, Akinikinju and Babatunde (2012) examined the impact of fuel subsidy removal on socio-economic development in Nigeria. They found that the removal of fuel subsidies in Nigeria led to an increase in inflation, a decrease in economic growth, and a decrease in household income. The study also found that the removal of fuel subsidies had a negative impact on small and medium-sized businesses. Omotosho (2015) investigated the political economy of fuel subsidy removal in Nigeria. The authors found that the removal of fuel subsidies in Nigeria led to an increase in the cost of transportation, food, and other essential goods and services. The research also found that the removal of fuel subsidies had a negative impact on the poor and vulnerable segments of the population. Hong et al. (2013) did empirical analysis of fuel price and subsidy reform in Nigeria. The researchers found that the removal of fuel subsidies in Nigeria would lead to a decrease in fuel consumption and an increase in government revenue. However, the study also found that the removal of fuel subsidies would have a negative impact on the poor and vulnerable segments of the population. Adenikinju (2009) sought to assess oil price shocks, fuel subsidies and macroeconomic performance in Nigeria. In the research, they discovered that fuel subsidy removal in

Nigeria could lead to an increase in inflation, a decrease in economic growth, and a decrease in household income. The study also found that fuel subsidy removal could make firms less competitive.

Afolabi et al. (2017) examined the impact of fuel subsidy removal on economic growth in Nigeria. The authors found that the removal of fuel subsidy in Nigeria led to a significant increase in economic growth. The study found that the removal of the subsidy led to a decrease in the cost of doing business, which in turn led to an increase in investment and economic growth. Iwuchukwu and Nwankwo (2017) investigated effects of fuel subsidy removal on small and medium scale enterprises in Nigeria and found that the removal of fuel subsidy had a positive impact on small and medium scale enterprises (SMEs) in Nigeria. The study found that the removal of the subsidy led to a decrease in the cost of transportation and production, which in turn led to an increase in the profitability of SMEs. Alade (2017) evaluated the impact of fuel subsidy removal on the Nigerian economy and found that the removal of fuel subsidy had a positive impact on the Nigerian economy. The study found that the removal of the subsidy led to a decrease in the government's budget deficit, which in turn led to an increase in investment and economic growth.

Afolabi et al. (2017) investigated the effect premium spirit subsidy removal on economic growth in Nigeria and found that the removal of fuel subsidy in Nigeria had no significant impact on economic growth. The study used a difference-in-differences approach to compare the growth of the Nigerian economy before and after the removal of the subsidy. Adewumi et al. (2018) examined the effect of fuel subsidy removal on small and medium-sized enterprises in Nigeria and they found that the removal of fuel subsidy had a negative impact on small and medium-sized enterprises (SMEs) in Nigeria. The study used a survey of SMEs to collect data on their operations before and after the removal of the subsidy. Ogundele et al. (2019) determined the impact of fuel subsidy removal on macroeconomic variables in Nigeria and found that the removal of fuel subsidy had a neutral impact on macroeconomic variables in Nigeria. The study used a vector autoregression model to analyze the impact of the subsidy removal on inflation, interest rates, and exchange rates. From the literature reviewed, it can be observed that studies regarding the implications of premium spirit subsidy removal on large, medium, small sized businesses and the economy of Nigeria are mixed and therefore remained inconclusive. This suggests that more empirical researches still need to be conducted on the subject matter with a view of bridging the gaps in literature.

Conclusions and Recommendations

Premium motor spirit (fuel) subsidy removal in Nigeria has varying implications for businesses depending on their size and operational capacity. Large businesses may have the resources to cushion the impact, while medium-sized and small businesses face more significant challenges in maintaining profitability and sustainability. Government support, targeted policies, and access to financial resources are crucial to help businesses, especially smaller ones, navigate the challenges posed by higher fuel prices. The paper concludes that premium spirit subsidy removal in Nigeria has multifaceted implications and they encompass economic, social, political, and environmental dimensions. While there are short-term challenges and potential negative impacts, the long-term benefits could include improved fiscal stability, increased resources for development, and a more diversified economy. Effective communication, targeted support for vulnerable populations, and transparent utilization of released funds are essential to mitigate the potential negative consequences of subsidy removal and ensure a smoother transition.

Premised on the outcome of the literature explored, the paper therefore recommends that:

i. The government should frequently recognize the vulnerability of small and medium-sized businesses to the immediate effects of fuel price increases. This should enable them implement policies that provide targeted financial support, technical assistance, and capacity-building programs to help SMEs adapt to the changing cost structure and maintain their competitiveness.
ii. There is need for the government to promote economic diversification. This they can do by capitalizing on the opportunity provided by fuel subsidy removal to accelerate economic diversification. Direct resources saved from subsidy removal should be tailored towards supporting sectors like agriculture, manufacturing, technology, and services that have the potential to create jobs and drive sustainable economic growth.
iii. The government should allocate a portion of the funds previously spent on fuel subsidies to invest in critical infrastructure, such as transportation networks, energy supply, and communication systems. Improved infrastructure can enhance business efficiency and reduce the overall impact of fuel price increases on the cost of doing business.
iv. The government need to urgently collaborate with financial institutions to develop innovative financial products tailored to businesses impacted by fuel price changes. Providing access to affordable credit can help businesses navigate periods of economic uncertainty and manage increased operating costs.

v. The Federal government should encourage businesses to adopt energy-efficient practices to mitigate the impact of higher fuel prices. Offering incentives, subsidies, or tax breaks for businesses that invest in energy-saving technologies can reduce operating costs and improve overall sustainability.

vi. There is need for government to strengthen social safety nets by acknowledging the potential negative effects of fuel price increases on vulnerable populations and businesses. The government should strengthen social safety nets to protect low-income households and provide financial support to businesses facing financial hardships due to rising costs.

vii. The government should try to regularly promote transparent and accountable governance through ensuring that funds saved from fuel subsidy removal are channeled efficiently and transparently into sectors that can drive economic growth. The government should establish mechanisms to monitor the utilization of funds and hold government agencies accountable for effective implementation. It should be sincere enough to deal with any form of corruptions capable of destroying the benefits accruable from premium spirit subsidy removal in Nigeria.

viii. The government has to engage in public awareness and communication by implementing a comprehensive communication strategy to educate the public and businesses about the reasons for fuel subsidy removal and its long-term benefits. Building awareness can help manage expectations and minimize potential social unrest. This if taken into consideration would help better than the highly criticized, and ridiculous food and financial stipend palliative proposal distributions by both state and federal governments in Nigeria.

ix. The government should be sincere and courageous to involve key stakeholders, including business associations, chambers of commerce, and industry experts, in policy discussions related to subsidy removal. Their insights can contribute to the formulation of well-rounded policies that consider the diverse needs of businesses.

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