Policyweekly

Why is Fuel Subsidy Removal Hurting Many Nigerians?

Examining Six Ways to Reduce the Pains

Policy Recommendations

1. The government should address widening inequality through investment in infrastructure with a target of reducing out-of-pocket expenditure.
2. There is a need to review minimum wage for civil servants to reflect the current economic realities.
3. Nigeria's tax system should be reformed to protect the poor and properly redistribute income.
4. The Nigerian government should scale up the fight against banditry and insurgency in order to provide a secure environment for farmers to return to their farmlands across the country.
5. There is a need to diversify the economy by investing parts of the proceeds of subsidy removal in other productive sectors of the economy.
6. The federal government should support local oil refining through modular refineries for enhanced efficiency.

Introduction

Fuel subsidy ended in Nigeria on 29th May 2023. The newly sworn-in President, Bola Ahmed Tinubu, subtly announced the end of subsidy by thanking the outgoing administration of Muhammadu Buhari for not including subsidy in the budget. In accordance with this statement, fuel prices tripled immediately, and by the third week of July, fuel prices went up by a further 15% to ₦617 (US$0.78) a litre. Previous administrations since 1999 made efforts to put an end to the fuel subsidy regime in Nigeria but were met with stiff resistance by the masses, sometimes supported and led by a section of elites in the opposition political parties.

To provide justification for subsidy removal, fuel subsidy has been proselytised as a waste of state resources which benefits the rich. President Tinubu alluded to this orthodoxy when he stated during his inaugural speech that "petrol subsidy regime... has increasingly favoured the rich more than the poor". However, the reality in Nigeria is that people with low incomes and the middle class are usually badly hit by fuel subsidy removal. In fact, some members of the middle-class risk being pushed down into poverty as a result of the fuel subsidy removal and the concomitant increase in the prices of commodities. For instance, following the increase in fuel prices since 29th May, analysts reported that food prices and transport fares increased by an average of 100 per cent across major cities in Nigeria.

The World Bank, itself an advocate of subsidy removal, remarked recently that poor and economically insecure households would suffer an estimated income loss of ₦5,700 per month as a result of subsidy removal. It added that, except palliatives are provided, additional 7.1 million Nigerians would become poor as a result of fuel subsidy removal. Corroborating this fear, in his later speech during the 2023 Nigeria's Democracy Day celebration, President Tinubu empathised with the suffering masses when he acknowledged that the fuel subsidy removal would impose a burden on the masses but noted that he felt their pains.

To mitigate the impact of fuel subsidy removal, especially on the poor, the current administration has proposed measures including a monthly payment of ₦8,000 (US$10) as a palliative to the poor. However, there are debates about the sustainability and adequacy of the proposed amount in mitigating the pains of fuel subsidy removal. There are also questions about the credibility of the social register to be relied upon for the distribution of the palliatives. Against the backdrop, this edition of Nextier SPD Policy Weekly x-rays the impact of fuel subsidy removal and provides actionable recommendations on policy, institutional and strategic interventions for mitigating the pains of subsidy removal.

Understanding the Real Reasons for Ending Fuel Subsidy Regime in Nigeria

Nigeria's fuel subsidy removal is explained by two key factors – the rentier character of the Nigerian state and the intensification of neoliberal reforms aimed at rolling back the state from the provision of basic services to the citizens. Nigeria is a rentier state which derives a substantial portion of its revenue from sales of crude oil to external clients. As a rentier state, Nigeria manifests symptoms of the Dutch Disease – a situation where a sudden influx of foreign exchange income (mainly sales of natural resources like crude oil) causes inflation and neglect of investment in other sectors of the economy (Okonjo-Iweala, 2012). Thus, since the discovery of oil in commercial quantity, agriculture has not only been displaced as a major revenue source but has continued to receive weak attention from the state, as demonstrated by the poor investment in agriculture and the concomitant fall in the contribution of agriculture to Nigeria's revenue. Agriculture as a share of the value of exports dropped from 75 per cent in 1965 (Okonjo-Iweala, 2012) to less than two per cent between 2016 and 2018.

As a rentier state, Nigeria is also characterised by a high cost of governance arising mainly from corruption and the over-bloated public sector. A study by the Nigerian Institute of Social and Economic Research (NISER) revealed that at least 80 per cent of public funds are appropriated as allowances and overheads by public officeholders who constitute less than five per cent of the population. Nigeria's high cost of governance and a lack of investment in other productive sectors of the economy have led to the growing budget deficit, rising debt profile of the country, and dwindling government revenue.

Nigeria's 2023 budget of ₦21.83 trillion has a deficit of ₦10.78 trillion, meaning that about 50 per cent of the budget will be funded through borrowing and sales of government assets. Worse still, a whopping ₦6.31 trillion, representing 29% of the total expenditure, has been budgeted for debt servicing. Nigeria spent 80% of its revenues on debt service in the first 11 months of 2022. The situation could be worse in 2023. The International Monetary Fund (IMF) warns that growing deficits will cause public debt to soar over the next four years unless the government increases revenue and brings down subsidies. Meanwhile, data from the Debt Management Office show that Nigeria's total debt stock as of 31 March 2023 stood at ₦49.85 trillion (US$108.29 billion). Nigeria's large budget deficit, the increasing national debt stock and low undiversified revenue base clearly suggest that the incoming administration would be in dire need of funds to sustain the rising cost of governance. This suggests why the new administration had to take the bold step to remove fuel subsidies despite criticisms from the masses.

The implementation of neoliberal reforms is another factor that explains Nigeria's subsidy removal. Since the return to civil rule in 1999, successive administrations have pursued subsidy removal as a cardinal pillar of the neoliberal reforms which is part of policy prescriptions by the Bretton Woods institutions to African countries. The World Bank has been at the forefront of the advocates for subsidy removal in Nigeria, stating that the money spent on subsidies could be channeled to other critical sectors. This explains why the Bank lauded the current administration for taking the bold step to end the fuel subsidy regime. The World Bank projected that Nigeria's GDP growth could double to over 4% by next year as a result of the subsidy removal and other related reforms. The World Bank is definitely gladdened by the implementation of its neoliberal reform principles in Nigeria. Could it be that the Bank is either unaware or refuses to acknowledge that the reform does more harm than good to the poor and the middle class?

Who is Fuel Subsidy Hurting in Nigeria, How and Why?

Nigeria's fuel subsidy removal hurts the poor and pushes the middle class into poverty. The World Bank disclosed that fuel subsidies would likely push additional 7.1 million persons into poverty. A 2022 report showed that Nigeria is home to 133 million persons who are multi-dimensionally poor. According to the World Bank, an additional four million Nigerians were pushed into poverty within the first five months of 2023. The socio-economic conditions of these millions of poor people will definitely worsen following fuel subsidy removal unless effective measures are put in place to cushion the impacts of fuel subsidy removal.

Nigeria's poor and middle class bear the burden of fuel subsidy removal because of many factors such as poor income/wealth redistribution mechanism and high rate of inequality; low minimum wage for workers; absence of infrastructure and basic amenities; and rising insecurity. Nigeria lacks effective mechanisms for efficient income/wealth redistribution. A report by the National Bureau of Statistics (NBS) puts Nigeria's Gini coefficient at 35.1, indicating a high inequality rate. This yawning gap between the rich and the poor in the country places the burden of fuel subsidy removal on the poor as they pay high fuel prices but cannot benefit from the wealth ostensibly saved through subsidy removal.

Again, the minimum wage of ₦30,000 monthly for civil servants was approved in 2019. However, this wage is not just poor but has not been reviewed following the removal of the fuel subsidy. This means that the salaries of civil servants remained constant while inflation occasioned by the fuel subsidy removal continued to soar, thereby reducing the capacity of the civil servants to meet basic needs with their wages. Further, the absence of basic infrastructure and amenities such as healthcare, good transportation system, affordable housing schemes etc., exposes the poor and middle class to sudden changes in prices connected to fuel subsidy removal. For instance, there is the prevalence of out-of-pocket expenditure in the area of healthcare, more than 90% of the Nigerian population is uninsured, and less than 5% of Nigerians in the formal sector are covered by the National Health Insurance Scheme (NHIS) established in 2006, only 3% of people in the informal sector are covered by voluntary private health insurance. Thus, with fuel subsidy removal, many Nigerians would have lesser disposable income to take care of basic needs such as healthcare.

The rising insecurity occasioned by violent conflict between farmers and herders, insurgency and banditry across the country are limiting livelihood sources and opportunities for the poor to upscale their income through agricultural activities. This lost opportunity deepens the impact of fuel subsidy removal on the poor, as many would find it difficult to commute to their farms or purchase food items from the markets, given the increased prices. Furthermore, the rising food insecurity due to the inability to access rural agro-communities means that food supplies are low, while demands, especially in urban slums and urban-rural areas where most of the middle and poor class live, are high.

Recommendations: Six Ways to Mitigate the Pains of Subsidy Removal

1.The government should address widening inequality through investment in infrastructure: As a long-term strategy of mitigating the impact of fuel subsidy removal on people with low incomes and the middle class, the new administration should invest the proceeds of subsidy removal to strengthen Nigeria's health system to reduce out-of-pocket expenditure. There should be more investment in pro-poor housing schemes to reduce household income spent on rent. The transportation system should be enhanced by building intercity rails for easy movement for the poor, particularly farmers and civil servants. To achieve the Infrastructure Support Fund (ISF) established by the new administration should be managed through a Public Private Partnership (PPP) system with built-in accountability measures.

2.Review minimum wage for civil servants: The minimum wage for civil servants should be reviewed to reflect the current economic realities. This will enable civil servants to cope with the fuel price increase and overall inflation.

3.Pro-poor tax system: Nigeria's tax system should be reformed to protect the poor and properly redistribute income. The multiple taxations suffered mainly by the poor should be addressed by synchronising the informal tax with the formal taxes levied primarily to operators in the informal sectors of the economy. To this end, the establishment of the Presidential Fiscal Policy and Tax Reform Committee by the new administration is in the right direction.

4.Address insecurity: The new administration should scale up the fight against banditry and insurgency in order to provide a secure environment for farmers to return to their farmlands across the country. There should be a deliberate security plan to safeguard and ringfence food basket communities to boost

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production. Strategic plans should accompany this on how to transport the food to where they are needed, thereby reducing post-harvest losses, which are on the rise due to the insecurity and fears of accessing such communities.

5.Diversify the economy: The new administration should take the bold step of beginning the diversification process by investing parts of the proceeds of subsidy removal in other productive sectors of the economy, such as energy and creating manufacturing sector funds for SMEs. This will boost local manufacturing and contribute to revenue generation.

6.Government should support the establishment/operation of modular refineries: the federal government should support local oil refining through modular refineries. This will reduce the importation of fuel, reduce monopoly in the downstream sector, save foreign exchange and possibly lower prices.

Conclusion

Nigeria's fuel subsidy removal hurts the poor and the middle class because of factors such as poor income/wealth redistribution mechanism and high rate of inequality; low minimum wage for workers; absence of infrastructure and basic amenities; and rising insecurity. Sustainable strategies to mitigate the impacts of subsidy removal on the poor must address the inequality in the country and economic diversification.

References

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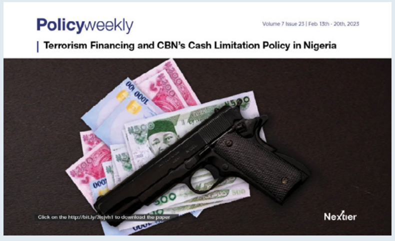

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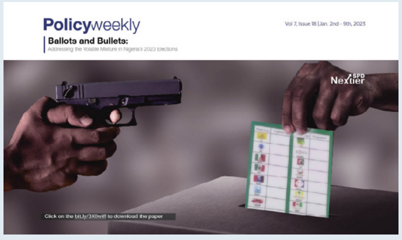

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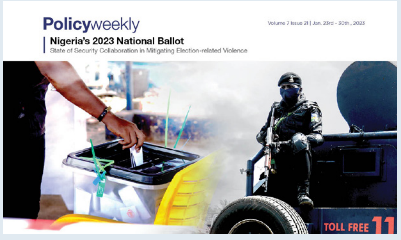

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