Fragile Balance of Payment Position: Policy Options

The net inflow of money into the Nigerian economy from other countries in Q4 2018 remained fragile and was dominated by oil and gas transactions. Clearly, the Nigerian economy is vulnerable to movements in the oil and gas market. FSDH Research makes this conclusion based on the latest report of the Central Bank of Nigeria (CBN) on the estimate of Balance of Payment (BOP) position of Nigeria as at Q4 2018. The weak BOP position buttresses the urgent need to create multiple sources of revenue and foreign exchange earnings for Nigeria.

Most countries around the world do business and financial transactions with other countries that require exchanges of money. These transactions are usually carried out by individuals or businesses, or by governments on behalf of their countries. The record of these transactions with other countries is known as BOP and is made up of three major components: Current Account, Financial Account and the Capital Account. The Current Account is usually the largest component of the BOP and it measures a country's trade balance plus the effects of net income and direct payments. The Financial Account measures the changes in domestic ownership of foreign assets and foreign ownership of domestic assets. The Capital Account is usually the smallest component of the BOP and it measures the financial transactions that do not affect a country's income, production, or savings. In some cases, Capital Account may be added to the Financial Account Transitions.

Just like the financial accounts of individuals and businesses, a country's BOP could be in a surplus or in deficit. Surplus means the country receives more money from other countries than it pays out. In Q4 2018, Nigeria recorded a surplus of US$2.8million lower than the surplus of US$6.18billion it recorded in the corresponding period of 2017 but higher than the deficit of US$4.52billion recorded in Q3 2018. Between Q3 2018 and Q4 2018, Nigeria was able to reduce its imports and increased its export of goods. The effect of these actions led to a significant reversal of Nigeria's
Current Account balance with its positive impact on the BOP. As in previous years, the main drivers of exports were crude oil and gas, representing 93.79% of total exports.

The Financial Account balance was in deficit during the period as more investments moved from Nigeria to other countries than they moved to Nigeria. Investments from other countries to Nigeria were dominated by portfolio investments attracted by good return in the financial sector, particularly in fixed income securities. FSDH Research stresses the need to improve the business environment in Nigeria to attract direct investment. This will create jobs, and ensure foreign currency stability and prosperity of the Nigerian economy. In the March 2019 edition of our Monthly Economic and Financial Market report entitled 'Economic Realities: Policy Options', we discussed strategies to improve the Nigerian business environment. Some of the policies we suggested include: reduction in administrative delays in obtaining licences and approvals, investment in infrastructure through partnership with the private sector, and removal of multiple exchange rate systems.

The CBN report shows that the position of external reserves as at Q4 2018 at US$42.59 billion was enough to cover 13 months of imports. This is higher than the 3 months global benchmark and 6 months West African Monetary Zone (WAMZ) benchmark. This also provides temporary stability for the value of the Naira. However, the long-term stability of the value of the currency will depend on the ability of the country to generate foreign exchange from multiple sources and to build domestic capacity to save, invest and consume goods and services that are produced locally.

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Sources: Central Bank of Nigeria (CBN) and FSDH Research Analysis
LHS: Left-Hand Side, RHS: Right-Hand Side
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