

Impact of Petroleum Subsidy on SSB Performance in Nigeria

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Abstract

This research evaluates the impact of fuel subsidy removal on small scale business, in Nigeria using Lagos, Enugu and Kano as case study. The study used the chi-square distribution analysis to estimate the effect. The study found that fuel subsidy removal had a negative impact on the performance of small scale businesses in Nigeria at the 5% level of significant. It also reveals that fuel is a very important input in the development of small scale businesses.

Background to the Study

Arrow (1985) opined that in economic theory, under certain circumstances, the allocation of resources by market forces is optimal. But this differs in practice, in the real world, market forces does not allocate resources efficiently. Hence, government intervenes by granting subsidies and other incentives to restore resource allocation to the efficient or optimal level. This has been the allocation rationale for the 23 years (1973-2003) of subsidy on Premium Motor Spirit (PMS or fuel) in Nigeria. Joseph (2012) asserted that fuel subsidy is the fund used by the government to keep down the price of fuel. This resulted in a pump price of #65/litre, low cost of transportation and reduction in the growth rate of inflation. The Small Scale Businesses (SSBs) are not left of; Oyedele (2012) identified Small Scale Businesses as the most beneficiaries of fuel subsidy. This has led to the growth of SSBs in Nigeria in recent times. As observed by Sanusi (2003) small scale business constitutes 85% of all firms operating in the economy.

The huge benefits of subsidy on fuel had its cost and social implications. There was an increase in budget deficit because of the increasing cost of financing the subsidies. Also, there were cases of large scale corruption in the oil industry that created artificial scarcity thus making the impact of fuel subsidy not to be felt. The Goodluck's administration, in attempt to curb these abnormalities in the oil industry announced the removal of fuel subsidy on the 1st of January 2012. This was to free up a total of #1.134 trillion to be reinvested into other sectors of the economy such as infrastructure, agriculture, health etc (Okonjo ,2012). The subsidy removal has generated heated debates across the various tiers of government, the academia, petroleum marketers and the masses who took to the streets in protest. The subsidy removal brought an increase in price from #65/litre to #140/litre, over 100% increase in price.

This change in fuel price will have an adverse effect on SSBs and ultimately the economy since they play important role in the development of the nation's economy. Wolfenson (2012) supported this claim by stressing that the small business sector is recognised as an important component of economic development and a crucial element in the effort to lift nations out of poverty. Based on the importance of SSBs in the economic growth of developing a nation like Nigeria, the study seeks to identify the effects of fuel subsidy on small scale businesses in Nigeria.

Statement of Problem

Small scale businesses are very important to any nation's economic growth. They are means through which accelerated economic growth and rapid industrialisation have been achieved in the industrial world. Fabayo (2009) opined that small scale businesses contribute to production in the producing sector, the service sector and facilitated trade in the trading sector. Over 90% of Nigerians are employed in the small scale business sector. These include okada transport (transport by motorcycle), hair salon, tailors, welders, and photocopiers and food vendors among others. They are faced with numerous problems that have inhibited their performance in recent times like poor finance and infrastructural problems.

Since most small scale businesses depend on fuel for their energy needs, a change (price rises) in the price of fuel would affect SSBs performance adversely. With the removal of fuel subsidy, there was an increase in the price of fuel per litre. Consequently, cost of doing business increased, profit fell, leading to a fall in national income and standard of living.

Thus, the study seeks to address the following research questions: What are the effects of fuel subsidy removal on small scale business? , and in what ways can the effect of fuel subsidy removal on small scale businesses be reduced? The broad objective of this research is to study the effects of fuel subsidy removal on small scales business in Nigeria. The Specific objectives of the study are to: Evaluate the effect of fuel subsidy removal on small scale businesses and Suggest ways to reduce the effect of fuel subsidy removal on small scale businesses.

Hypothesis of the Study: The hypotheses to be tested in the course of this research are;

Ho: Fuel subsidy removal has no significant effect on SSBs in Nigeria.

H1: Fuel subsidy removal has significant effect on SSBs in Nigeria.

Theoretical framework: The study adopted the free market economy as its theoretical framework. The free market economy model is based on laissez-faire, economic liberalism and free trade respectively. Laissez-faire was advocated by Adam Smith who believed that when there is competition, the market invisible hand would lead to proper pricing and it played a great role in determining economic policy recommendation; they therefore strongly opposed any government interference with business affairs. Trade restrictions, minimum wage laws and subsidy were all seen as detrimental to economic wellbeing. In recent times, the government has tended towards economic liberalism and deregulation which involves the cancellation of subsidies. This is a shift from government regulation to a free market mechanism of the invisible hands; this is evident in the privatisation and commercialisation of public enterprises since 1980. Hence the study assesses the effect of government drives towards a free market system by the removal of fuel subsidy on small scale business and suggest a way of curbing the effects that aims along with it.

Empirical Literature review:

Obokoh and Lawrence (2008), using a sample of 500 manufacturing SSBs discovered that SSBs does not feel the positive effect of liberalisation due to improper planning and absence investment climate. Akinlo and Odusola (2003) discovered from their study on the effect of trade liberalisation on SSBs that there was a decrease in turn over. They attributed this to two main reasons, Accumulated inventory due to low demand occasioned by fall in the income of the population as a result of the subsidy removal and increase cost of production affecting the profit potential. Ekpeyong (2002) studied the impact of structural Adjustment programme (SAP) on SMEs in Nigerians following the high inflation. Agboli and Ukaegbu (2006) found from their study that trade policy led to low budgetary allocation for infrastructure management by government, leading to deplorable infrastructure and causing small scale business to spend on those infrastructures. Sanusi and Adelaja (2003) using a simple random sampling technique to study 200 SMEs identified inadequate finance, shortage of skilled manpower and lack of infrastructural facilities as the major problems of SSBs in Nigeria. Olabisi et al (2007) surveyed 211 business owners to study the informal economy of Lagos state discover that the constraints hindering small scale business growth and survival are corruption, lack of experience, poor infrastructure, insufficient profit and low demand for product and service. Adeola (2005) used a random sample of 50 SMEs to study the cost of power outage to the business sector found that the poor state of electricity supply imposed significant cost on the business sector and stated further that most SMEs fail due to their inability to finance their back up power. David et al (1992) used the interview approach to study the characteristics of 150 small scale businesses in Nigeria and pointed out that 8 out of every 10 businesses (80%) were failing. Eme and Okechuku (2011) used a 34 years (1973-2007) time series data to study deregulation in Nigeria showed instability of fuel prices, high rate of inflation and unemployment occasioned by the fuel subsidy removal. This also had negative effect on SSB performance. Ismaila (2012) surveyed 1600 SMEs made up of agro allied and non-agro allied industry and analysed the result using the Standard Package Statistical Software (SPSS) and found that SMEs is prerequisite for employment generation in Nigeria. Anthony (2012) used the Ordinary Least Square method (OLS) to study policy support and SMEs performance discovered that of the three study variables, technology and financial support impact SMEs positively while infrastructural support is negatively related to SMEs performance.

Methodology: The study uses a multi stage random sampling technique. Out of the three states in Nigeria (Lagos, Enugu and Kano) were randomly selected. Subsequently, two major commercial centres were randomly selected out of the states (in Lagos, Aswani and Palmgroove business area, Ogbete and new market in Enugu and Sabon Tasha and Bata in Kano respectively). A total of 50 questionnaires were randomly distributed in the two business areas respectively. The questionnaires were carefully constructed and designed to elicit responses from SSBs operators.

Method of data analysis: Chi-square would be used for presentation and analysis of data. The chi-square formula is stated as

$$X^2 = \sum \frac{(F_o - F_e)^2}{F_e}$$

Where X^2 = calculated chi-square, F_o = observed frequency and

F_e = expected frequency. The degree of freedom = $(r-1)(c-1)$. Where: r = number of rows. C = number of columns. The critical value of X^2 is 0.05 (from table) at 95% level of significance.

TABLE 1 SHOWS THE CHI-SQUARE(X^2) COMPUTATION.

Responses	Observed Frequency(F_o)	Expected Frequency(F_e)	$F_o - F_e$	$(F_o - F_e)^2$	$\frac{\sum(F_o - F_e)^2}{F_e}$
Yes	204	80	124	15376	192.20
No	24	80	-56	3136	39.20
Undecided	12	80	-68	4624	57.80
Total	240	240			289.20

Source: Field Survey, 2012.

From table 1, the null hypothesis is tested. The three questions served as the number of rows and the alternatives are the number of columns. The degree of freedom (DF) = (r-1) (c-1)

$$DF = (3-1) (2-1)$$

$$DF = 2 \times 1 = 2.$$

The standard chi square table value of 2 DF (at 5% level of significance) is 5.99. Since the calculated value of chi square is greater than the tabulated critical value ($289.20 > 9.49$), the researcher therefore reject the null hypothesis and accept the alternative thereby restating that the removal of fuel subsidy has a significant impact on the performance of small scale businesses in Nigeria.

Policy implication of findings: It can be deduced from the foregoing analysis that fuel is an important source of energy for small scale business, given that the alternative which is Electricity, supplied by the power holding company of Nigeria (PHCN) is not very efficient. Hence, the removal of fuel subsidy created significant increase in the cost of business operation, fall in sales, level of stock and profitability of the small scale business (See attached).

The study also revealed that finance and energy are the major problems affecting SSBs performance. Hence, with the phase out of subsidy on petroleum, the government should work on boosting efficient supply of electricity as well as development of other costless and environmentally friendly sources of energy. The problem of finance should also be tackled by creation of accessible loans for small scale business owners.

More importantly, the Subsidy Reinvestment Programme initiated by the government to cushion the effect of fuel subsidy removal should be duly implemented to meet small scale business owners.

Recommendations: Since it has been established that the small scale business is vital for economic Growth, development and achieving poverty reduction and employment generation, there is clear need to ensure that small scale businesses are not adversely affected by economic policies. Based on the findings of this study, the following recommendations are drawn;

- The federal government should provide some form of market protection for small scale businesses, so that their owners are not adversely affected by the deregulation of the petroleum industry.
- The government should work on efficient electric supply in both the rural and urban areas to cut the high cost of energy supply, as well as developing other sources of energy like solar and bio-gas.
- The government should put up policies that would enhance the accessibility of small business owners to credit facilities to boost their performance.
- The government should pursue the development of critical infrastructures like road, bridges, drainages and warehousing facilities, which added significant cost to the business owners.
- The federal government should also ensure that the subsidy reinvestment programme meet the targeted small scale business owners. By this, a special monitoring committee should be set up and mandated to follow up and evaluate the performance of the program.

Conclusion

The major objective of this research is to estimate the impact of fuel subsidy removal on small scale businesses in Nigeria. Based on the findings, it is concluded that the removal of fuel subsidies has a significantly negative impact on small scale businesses. The removal of fuel subsidy had significantly affected their level of stock, sales, their operation cost and ultimately their profit level negatively.

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