

PETROLEUM SUBSIDY REMOVAL AND THE OPERATIONAL COST OF SMALL AND MEDIUM ENTERPRISES IN KOGI EAST SENATORIAL DISTRICT, KOGI STATE

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ABSTRACT

This paper examined the effect of petroleum subsidy removal on the operational cost of small and medium enterprises in Kogi east senatorial district, Kogi state. The survey research method was employed to gather information and data from both primary sources. A structured questionnaire was administered to a sample of 500 respondents selected from a population of 5000. Multiple regression was used in testing the hypotheses. It was found that exchange rate fluctuations has positive beta coefficient (0.569) with a p-value of (0.000) showing a strong statistical significant relationship with operational cost of small and medium enterprises in Kogi east senatorial district, Kogi state. It was also revealed that petroleum price hike has positive (0.590) and significant p-value of (0.000.) with performance of small medium enterprises in Kogi east senatorial district, Kogi state. The study concluded that subsidy removal has positive and significant effect on the operational cost of SMEs in Kogi east senatorial district, Kogi state. The study recommended that SMEs should consider implementing hedging strategies like forward contracts or options to manage exposure to exchange rate fluctuations, enabling SMEs to control operational costs and maintain financial stability. It was also recommended that SMEs should adopt alternative technologies to reduce reliance on petroleum-based inputs, enhancing resilience against price volatility.

Keywords: Subsidy removal, exchange rate fluctuations, petroleum price hike, SMEs, operational cost.

INTRODUCTION

Petroleum subsidy removal refers to the government's decision to eliminate or reduce subsidies provided to consumers or producers in the petroleum sector. This policy change often involves discontinuing financial assistance or price controls that artificially lower the cost of petroleum-based products such as gasoline, diesel, and cooking gas. Petroleum subsidy removal aims to reduce fiscal burdens, promote market efficiency, and address budget deficits by allowing fuel prices to be determined by market forces rather than government intervention. However, it can lead to higher fuel prices, inflationary pressures, and socio-economic impacts, particularly on low-income households and transportation costs (Mishkin & Eakins, 2016).

The purchasing power of 85% of the population in the country has been adversely affected, leading to high unemployment rates. The issue of dollarization has exacerbated economic hardships for the masses in Nigeria. Since 2016, Nigeria has experienced persistently high unemployment rates, significantly impacting its socioeconomic development. According to the National Bureau of Statistics (Popoola,

2020), the unemployment rate reached a concerning low of 23.1% in 2018, compared to a mere 2.3% between 1962 and 1985.

This problem is primarily attributed to the overreliance on oil by the Nigerian economy. The lack of reliable electricity supply has rendered many businesses unable to survive without resorting to generators to power their operations (Olawale, 2013). Exchange rate fluctuations refer to the changes in the value of one currency relative to another over a period of time. These fluctuations occur due to various factors such as changes in supply and demand for currencies, economic indicators, geopolitical events, and government policies.

Exchange rate fluctuations can impact international trade, investment, inflation, and the overall economic performance of a country. For businesses engaged in international trade or those dependent on imported/exported goods and services, exchange rate fluctuations can directly affect their costs, revenues, and competitiveness in the global market.

A fuel hike in price refers to an increase in the cost of fuel, such as gasoline or diesel. This increase can occur due to a variety of factors, including changes in global oil prices, shifts in supply and demand dynamics, fluctuations in currency exchange rates, geopolitical tensions affecting oil-producing regions, and government taxation or subsidy policies. A fuel price hike can have wide-reaching effects on the economy, as it can lead to increased transportation costs, higher prices for goods and services, inflationary pressures, and reduced consumer purchasing power (Miller & VanHoose, 2017). Additionally, industries that rely heavily on fuel, such as transportation, logistics, and manufacturing, may experience increased operational costs, which can impact their profitability and competitiveness.

The government opted to eliminate the subsidy on petrol due to the price gap of petroleum products in the market, aiming to alleviate the burden on the people. However, since the subsidy removal in 2023, Nigerians have experienced significant suffering across various sectors of the economy. This removal has imposed severe hardships on approximately 96% of the population. Despite the government's expenditure of over USD 3.9 Billion to mitigate the petroleum product prices for the masses, a faction of Nigerians, driven by greed and corruption, has exploited the government for their personal gain (Munshi, 2018).

While reducing operational cost is essential for SMEs to remain competitive and sustainable, it comes with associated costs and implications. By carefully assessing the costs and benefits of operational performance enhancement initiatives, SMEs can make informed decisions, allocate resources effectively, and achieve their strategic objectives.

However, the government's expenditure on subsidy removal surpasses its investment in other sectors crucial for a sustainable economy and the well-being of Nigerians (Hafez, 2018). The elimination of subsidies in Nigeria has stirred palpable tension among the populace, leading to increased petroleum prices in the market and fluctuations in the exchange rates of the dollar and pound. Consequently,

inflation trends have risen, significantly impacting the costs of production, education, transportation, and consumable goods and services. These challenges form the basis of the problem statement in this study. Both the research conducted by Sam et al. (2014) and Emmanuel et al. (2019) utilized time series analysis to collect data spanning a 38-year period (1981–2018), focusing on the contributions of exchange rate (EXR), inflation (INF), and interest rate (INTR). However, this also highlights a gap in the current study.

The main objective of this study is to ascertain the effect of petroleum subsidy removal on the operational cost of selected small and medium scale enterprises in Kogi East Senatorial District, Kogi State. Other specific objectives are:

- i. To ascertain the effect of exchange rate fluctuations on the operational cost of SMEs in Kogi East Senatorial District, Kogi State.
- ii. To ascertain the effect of petroleum product price hike on the operational cost of SMEs in Kogi East Senatorial District, Kogi State Nigeria.

The following are research questions for the study:

- i. To what extent does petroleum exchange rate fluctuations affect the operational cost of SMEs in Kogi East Senatorial District, Kogi State Nigeria?
- ii. To what extent does price hike affect the operational cost of SMEs in Kogi East Senatorial District, Kogi State Nigeria?

The following hypotheses were formulated for the study:

Ho : There is no positive significant relationship between exchange rate fluctuations and the operational cost of SMEs in Kogi East Senatorial District, Kogi State.

Ho: There is no positive significant relationship between petroleum price hike and the operational cost of SMEs in Kogi East Senatorial District, Kogi State.

REVIEW OF RELATED LITERATURE

Concept of Subsidy Removal

Subsidy is defined as the process through which government raise financial support to relief masses and other sectors in order to bring down the price of fuel to meet the expectation of users in Nigeria (Scott & Kvilhaug, 2022). According to IMF (2020), subsidies can take different dimensions including tax rebate, soft loan in different amount, price stability regime and making availability of goods and services to people for stability of economic growth and development. While Haley and Haley (2013) opined that subsidies could be in form of tax free or relief, free cash transfer, and abysmal low interest rate on loan to cushion the effect of subsidy removal in the future endeavor.

The various form of subsidies is to reduce cost of production, improve the availability of goods and service and a well define investment opportunity. Prior to the subsidy removal regime, Nigeria had a subsidy system characterized by compensating for the gap between the actual retail price of petrol, determined through calculating the landing cost and existing margins. The second subsidy covers transportation expenses, amounting to approximately N30 per liter, to maintain consistent petrol prices nationwide (Akanbi, 2023). The fundamental purpose of subsidizing petroleum products is to maintain price stability and alleviate the burden of high fuel prices on consumer goods. However, the removal of subsidies in Nigeria has resulted in the adverse consequence of elevated petroleum product prices (Soremekun, 2023).

Popoola (2020) argued that petroleum subsidies were introduced in Nigeria to uphold price stability and prevent unjustified surges in petroleum prices in the market. This measure aimed to maintain stability in the transportation sector. Munshi (2018) underscores the financial difficulties associated with subsidies, which have led to rampant corruption and mismanagement of the nation's treasury. A significant portion of funds was allocated to subsidies, while other sectors received lesser amounts. The government's substantial investment in subsidies aimed to lower fuel prices for the people. However, it became evident that this allocation was a tremendous waste of resources due to mismanagement and corruption among stakeholders.

Fluctuation of Exchange Rates

The fluctuation of exchange rates refers to the periodic and unpredictable changes in the value of one currency relative to another in the foreign exchange market. These fluctuations occur due to various factors such as changes in supply and demand, economic indicators, geopolitical events, and government policies, impacting the purchasing power of currencies and affecting international trade, investment, and financial transactions (Madura, 2020).

The fluctuations in exchange rates, oil prices, and gross domestic product (GDP) have posed significant challenges to the growth of Nigeria's economy. The increase in the value of the dollar in Nigeria following the removal of subsidies has impacted the prices of petroleum products and other goods and services in the market. This rise in exchange rates has led to an increase in oil prices, thereby reducing the purchasing power of individuals in society while showing growth in the gross domestic product (GDP). Nigeria's exchange rate, oil prices, and GDP exhibited rising trends from 1960 to 1970, followed by a subsequent decline. The annual average growth rates from 1970 to 1974, 1980 to 1985, 1990 to 1994, and 2000 to 2010 consistently recorded economic growth and sustainability.

Petroleum Price Hike

A petroleum price hike refers to a sudden and significant increase in the cost of petroleum-based products, such as gasoline, diesel, and heating oil. This increase is typically driven by factors such as rising crude oil prices, changes in global supply and demand dynamics, geopolitical tensions, and government policies related to taxation and regulation. Petroleum price hikes have widespread economic implications, affecting consumer spending, transportation costs, inflation rates, and overall economic stability (Miller & VanHoose, 2017).

The escalation of fuel prices has emerged as a widespread concern following the removal of subsidies on petroleum products in Nigeria, significantly impacting the country's economic activities. The rise in petroleum prices has led to increased transportation costs, higher prices of goods and services in the market, and a surge in wage demands by the Nigeria Labour Congress. These developments have had detrimental effects on Nigeria's economic prospects. If this trend of unusual price hikes continues unabated, it could exacerbate hardships for the populace, potentially leading to social unrest within the country.

The prevalence of corruption and mismanagement within the oil industry has hindered its operational efficiency, rendering the efforts implemented by the NNPC futile due to the involvement of various stakeholders in the country (Jack, 2011). These stakeholders have greatly benefited from corrupt practices within the oil industry. Between January and March 1999, there was a notable surge in local daily consumption and imported liters of fuel, which had a positive and significant impact on Nigeria's GDP growth. Allwell (2012) proposed that major stakeholders in the oil industry, as well as smugglers and saboteurs, often orchestrate artificial scarcity to drive up fuel prices in Nigeria. During this period, the country experienced severe fuel shortages, with the black market thriving as the primary means of defrauding consumers. Arinze (2011) argued that such fuel scarcities inflict considerable hardships on the masses and serve as indicators of mismanagement of the nation's resources.

Despite the adverse effects of fuel price hikes, the Federal Government of Nigeria ceased petroleum subsidies on January 1st, 2012. However, there are economic ramifications associated with fuel price increases within the system, which the Nigerian government must now address or confront in the near future. Osogie (2012) further suggested that the rise in petrol prices resulting from subsidy removal would likely lead to inflation and a depreciation in the value of the minimum wage in the country.

Operational Cost of SMEs

The operational performance of Small and Medium Enterprises (SMEs) is crucial for their success and sustainability in competitive markets. However, achieving and maintaining high operational performance often comes with associated costs. These costs are involved in enhancing and maintaining the operational performance of SMEs, examining various aspects and implications. Adopting and integrating new technologies into SME operations often requires significant upfront investment in hardware, software, and infrastructure (Yan et al., 2020).

While such investments can improve efficiency and productivity in the long run, SMEs must bear the initial costs of implementation and training. Enhancing operational performance often necessitates upskilling or retraining employees to adapt to new processes, technologies, or quality standards (Abdullah et al., 2020). SMEs incur costs related to training programs, workshops, seminars, and hiring external consultants to build employees' capabilities. Improving supply chain efficiency and resilience often involves investment in advanced inventory management systems, transportation optimization tools, and

supplier relationship management platforms (Bach, 2019). SMEs incur costs related to software licenses, consultancy fees, and supply chain restructuring efforts.

Theoretical Framework

The underpinning theory for this study is the dynamic model theory. This model delineates typologies of subsidies in terms of cost-effectiveness. Past literature, as cited in the work of Parish and McLaren (1982), critically examined this model, highlighting that subsidy payments primarily focused on the production of units of output and input without considering other variables that could enhance operational improvement. Variables such as dynamic and static models were utilized to demonstrate the operational performance and results, prioritizing factors beyond mere production.

The analysis revealed that the dynamic model proved more effective than the static model when considering inputs in relation to subsidies. Essentially, the dynamic model allows the government to adjust subsidy payments according to units of production comprehensively, thereby averting the wastage of national resources. It is therefore advisable for governments to adopt the dynamic model to ensure efficient subsidy payments and mitigate fraudulent practices. The government's inability to determine the appropriate model for subsidy payment led to confusion, resulting in the cessation of payments and ultimately the removal of subsidies in 2023. This decision allowed market forces to dictate prices, aiming to restore equilibrium and efficiency.

Empirical Review

Chien-Chiang (2023) examined the impact of China's exchange rate policy uncertainty on manufacturing firm performance. Using the fixed effect model and quantile regression model. The results show that a fluctuating exchange rate policy is detrimental to lower performing corporates but constrains higher performing ones. The beneficial benefit seems to be explained by government subsidy, and business governance, expansion, and financial restrictions either amplify or mitigate the effect. The volatility of exchange rate policies also puts a great pressure on corporations to modernize and adapt their businesses, which boosts their performance correspondingly. Furthermore, it has been observed that positive shocks greatly enhance corporate performance, whereas negative shocks, such as the global financial crisis and the COVID-19 outbreak, impede corporate growth. All things considered, Chinese manufacturing companies' risk confrontation ability is on the rise. Therefore, the Chinese government ought to implement more favorable exchange rate policies in order to boost market sentiment and promote greater openness in the country's industrial sector. More corporate-friendly policies might be introduced, like prompt adjustments to manufacturing company subsidies and assistance in addressing exchange rate policy uncertainty issues for more established manufacturing firms.

Emmanuel et al. (2019) used the ARDL approach to study the long-term association between the exchange rate and the performance of small and medium-sized businesses in Nigeria. The study used time series analysis to gather data on the 38-year period (1981–2018) contributions of exchange rate (EXR), inflation (INF), interest rate (INTR), and output of the wholesale and retail trade to GDP (a proxy for the performance of small and medium enterprises, PSME). To analyze the data, both analytical and descriptive tools were used. The performance of SMEs in Nigeria was found to be correlated over the long term with the currency rate using the Autoregressive Distributed Lag model. Interest rates and

inflation rates were added to the exchange rate. According to the estimated ARDL model's results, the present period has seen a recovery of the prior periods' disequilibrium by approximately 8.01% of the adjustment speed. The results show that the exchange rate (EXR) has positive but negligible long-term effects on small and medium-sized enterprises (PSME), while the inflation rate (INF) and interest rate (INTR) have significant long-term negative and positive effects, respectively, on PSME performance (performance contributions of wholesale and retail trades to GDP as a proxy). This suggests that, over time, exchange rate fluctuations have little effect on the performance of SMEs. The study concludes that robust policies that would preserve a favorable and stable exchange rate must be developed by the federal government, the Central Bank of Nigeria.

Sam et al. (2014) conduct empirical research on how petroleum affects the growth of small and medium-sized businesses (SMEs) in Nigeria. To investigate the effects of petroleum pricing (PP), imported petroleum (IMP), and domestically produced petroleum (DPP) on Nigeria's small and medium-sized enterprises (SMEs), the log linear error correction model was utilized. To ascertain each variable's degree of stationarity, a unit root test was performed. It was safe to move forward with the Johansen Cointegration Test after they were discovered to be stationary after the first difference, meaning that they are all integrated of order one (I(1)). Regression analysis was then performed using the integrated variables. The cointegration result demonstrated the long-term, or equilibrium, link between the model's variables. The investigation revealed that DPP had a favorable impact and is statistically significant, whereas PP and IMP were found to be statistically insignificant and had negative correlations with the development of SMEs in Nigeria. The government of Nigeria had to import the excess due to the underproduction of its petroleum refineries, which has an impact on the product's sales and distribution costs. Transporting their products and services to the markets required local farmers and manufacturers to pay more. Petroleum product price increases that never stop have sparked a crisis and industrial actions in Nigeria spearheaded by some pressure groups, which over time have distorted the country's small and medium-sized enterprise (SME) sector. According to the report, deregulating the downstream oil market would enable private investors to construct additional refineries and manufacture petroleum at a comparatively lower cost, which would support the expansion of SMEs throughout the nation.

Ilham et al. (2014) looked into the effects of growing fuel subsidies on sectoral and regional performance. Transportation and industrial sectors are the regional sectors most directly impacted by rising fuel prices, while sectoral performance—which can result in the development of value-added industries—saw a decline over the long and short terms. Firmly committed to lowering the burden of government expenditure in the budget and using funds for other uses, such as development. However, the increase in fuel prices will undoubtedly cause a spiral effect. The price of all goods and services will rise, creating a spiral effect. On the downside, this means that the sector's activity within the economy is inextricably linked to that of other sectors, meaning that sector-specific policies will have an impact on regional issues, which will then have an impact on the macro economy.

METHODOLOGY

This study investigated the impact of subsidy removal on the operational cost of small and medium-scale enterprises (SMEs) in Kogi East Senatorial District, Kogi State. Data were gathered from various

Table 1

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.180 ^a	.052	.033	.78094

a. Predictors: (Constant), Petroleum Price Hike (PPH) and Exchange rate Fluctuations (ERF)

Table 1a The multiple regression as shown the analysis of the impact of subsidy removal on the operational cost of SMEs in Kogi east senatorial district, Kogi state indicated two independent variables that is petroleum price hike (PPH) and exchange rate fluctuations (ERF) used to predict the value of the dependent as operational cost of SMEs (OCSMEs) in the Kogi east senatorial district, Kogi state. The results as indicated in Table 1 showed that the regression coefficient (R) and the coefficient of determination (R Square) is .052 (i.e. 52%). This means that a positive or partial-linear relationship exist between the dependent and independent variables

Table 2 ANOVA^b

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	5.207	2	5.307	7.338	.000 ^a
	Residual	113.648	178	.679		
	Total	117.854	189			

a. Predictors: (Constant), Petroleum price hike (PPH) and Exchange rate fluctuations (ERF)

b. Dependent Variable: Operational cost of SMEs (OCSMEs)

The variance of ANOVA shows that the regression model revealed F-value of 7.338. This implies that the petroleum price hike is a function of performance of SMEs. Thus, the two independent variables are best defining the dependent variable.

Table 3 Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.660	.253		.64.103	.000
	ERF	.5740	.67.8	.569	62.622	.000
	PPH	.554	.057	.590	.44415	.000

a. Dependent Variable: Performance of OCSMEs

Coefficients model of T-test revealed that, at 0.05 level of significance, relationship that exists between petroleum price hike and operational cost of SMEs (t=62.622, .44415 p>.05) is statistically significant.

In this case, a positive coefficient indicates a positive relationship between the exchange rate fluctuations and the operational cost of SMEs.

The findings reveal that fluctuations in exchange rates exert a positive and significant impact on the operational costs of SMEs, as evidenced by a p-value of less than .05 (.000). The Standardized

Coefficient (Beta) of .569 indicates that a rise in exchange rate fluctuations corresponds to a one-unit increase in SME operational costs. The result refutes the null hypotheses which states that there is no positive significant relationship between exchange rate fluctuation and the operational cost of SMEs in Kogi East Senatorial District, Kogi State. The result further proves that there is a positive and significant relationship between exchange rate fluctuation and the operational cost of SMEs in Kogi East Senatorial District, Kogi State. The findings is in tandem with the result of Emmanuel et al. (2019).

Similarly, the analysis demonstrates that a hike in Petroleum prices also has a positive and significant influence on SME operational costs, supported by a p-value of less than .05 (.000). The Standardized Coefficient (Beta) of .590 suggests that a one-unit increase in Petroleum prices results in a corresponding increase in SME operational costs. Based on the result obtained, the null hypothesis which states that there is no positive and significant relationship between petroleum price hike and the operational cost of SMEs in Kogi East Senatorial District, Kogi State is hereby rejected. This result aligns with the findings of Ilham et al. (2014).

CONCLUSION AND RECOMMENDATIONS

The core aim of this study is to appraise the impact of subsidy removal on the operational cost of small and medium enterprises in kogi east senatorial district, kogi state. The study take cognizance of subsidy removal by proxy of petroleum price hike and exchange rate fluctuations against the dependable variable of p operational cost of small and medium enterprises. The findings revealed that both the proxy of independent variables such as petroleum price hike and exchange rates fluctuations are major determinant of dependent variable via operational cost of small and medium scale enterprises. This means that the removal of subsidy has affected the economic activities in the country which resulted to upsurge increase in price of fuel, cost of goods and services, high cost of living and cost of transportation. The study has the following recommendations:

- i. SMEs should consider implementing hedging strategies like forward contracts or options to manage exposure to exchange rate fluctuations, enabling SMEs to control operational costs and maintain financial stability.
- ii. SMEs should adopt alternative technologies to reduce reliance on petroleum-based inputs, enhancing resilience against price volatility. By diversifying, SMEs can mitigate the impact of petroleum price fluctuations, bolstering competitiveness.

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