



Nigeria's Dwindling Revenue and Reserves in the face of Rising Oil Price

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The Context

For the second year running, prices in the global oil market have maintained an upward trend following the relaxation of lockdown measures, full resumption of economic activities and recently, the Russia-Ukraine crisis. Consequently, the average price of Bonny Light crude increased from US\$42.1 per barrel (pb) in 2020 to US\$71.1pb in 2021. As at February 2022, the average Bonny Light oil price has increased to US\$94.4pb. Contrary to expectation, the rising oil price has not significantly impacted Nigeria's economy. Rather, oil revenue and foreign reserves have continued to decline. Federally collected revenue as at November 2021 underperformed the projected benchmark by 47.4 percent and was lower than the 2020 figure by 31.1 percent. Likewise, the external reserves have been declining for most of 2021. Though the US\$4 billion issuance of Eurobonds in September 2021 helped to shore up the reserves, the reserves have maintained a steady decline since then.

While other oil-exporting countries are recording tremendous economic advantage from the rising oil prices, the case is reverse for Nigeria. For instance, Saudi Aramco, the government owned oil and gas company in Saudi Arabia, declared a 124 percent increase in profit to US\$110 billion in 2021, reflecting the level of inflows¹. Also, in Q4-2021, Saudi Arabia's oil sector expanded by 10.8 percent². In the case of Nigeria, however, the oil sector in Q4-2021 contracted by 8.1 percent and remained in recession. In accordance, the economy lost an estimated US\$14.26 billion in 2021, while the government lost US\$7.5 billion in oil revenue³. In addition, Nigeria lost about US\$15 billion in foreign reserves. Already in the first two months of 2022, Nigeria has lost US\$2.18 billion in oil revenue⁴. If Nigeria had secured these inflows as expected, the government could have borrowed much less than the N6.64 trillion debt accumulated in 2021⁵. The situation is quite worrisome: nevertheless, there are numerous opportunities for Nigeria, with the current situation in the global energy market.

¹ Aramco (2022). Financial Statement Full Year 2021. Retrieved from <https://www.aramco.com/en/news-media/news/2022/aramco-announces-fy2021-results>

² Saudi Arabia General Authority of Statistics (2022). Gross Domestic Product Fourth Quarter of 2021. Retrieved from <https://www.stats.gov.sa/sites/default/files/GDP%20FQ42021EN.pdf>

³ Internal estimate

⁴ Internal estimate

⁵ Debt Management Office of Nigeria (2022). Public Debt Data 2021. Retrieved from <https://www.dmo.gov.ng/debt-profile/total-public-debt>

What are the Issues and Challenges?

The NESG identifies four (4) interrelated buckets of challenges facing Nigeria's oil and gas sector that drive down inflows from the oil price increase. These include:

» **Low Crude Oil Production**

Nigeria's crude oil production has remained below budgeted levels since the third quarter of 2020. This could be partly attributed to issues around the enforcement of OPEC Quota, shut down of oil wells, oil theft, pipeline vandalism, illegal pipelines, etc. Due to the fallout of COVID-19 on oil price in 2020, the OPEC and OPEC+ members agreed to a supply cut with a quota for every member country. The OPEC quota for Nigeria continues to fall below Nigeria's installed capacity of 2.5 mbpd. While this inhibits production capacity, for most of 2021, Nigeria's production (excluding condensate) underperformed the OPEC quota. The OPEC quota for 2021 averaged 1.6 mbpd, while Nigeria's crude oil production (less condensate) averaged 1.31 mbpd, suggesting the existence of domestic constraints. Notably, the impact of the COVID19 pandemic on the sector still endures as many oil wells that were shut down during the peak of the pandemic are still struggling to return to operation. As at 2021, Nigeria's active rig count declined to seven (7) from 16 and 11 in 2019 and 2020, respectively. These have impacted Nigeria's capacity to produce and expand crude oil output.

In addition, insecurity is a major challenge facing the oil and gas sector in Nigeria. Issues of oil theft, pipeline vandalism, illegal pipelines, and oil exploration have resulted in significant output loss. While the activities of the Niger Delta militant groups have doused reasonably, oil theft has taken centre stage. Several pipelines in the country lose about 80 to 90 percent of their injections to vandals and oil theft before getting to the terminal, especially in the country's southeast region. For instance, about 95 percent of the produce in the Trans-Niger Pipeline is being hijacked: likewise, those leading to the Bonny Terminal. Other major targets of oil hijackers include the ENI-operated pipeline to the Brass terminal, the AITEO Nembe Creek Trunkline, Chevron's Escravos, the TransForcados pipeline. The outputs of oil companies and the NNPC

Limited/Joint Venture are being sabotaged, thus, gruesomely suppressing Nigeria's crude oil production level and limiting Nigeria's advantage from the oil price increase.

» **Dwindling Investment**

The passage of the Petroleum Industry Act (PIA) 2021 by the Nigerian government is commendable. The Act has the prospect to drive investment growth in the oil and gas sector if adequately implemented. Meanwhile, over the past four decades, Nigeria has not been able to expand crude oil production capacity beyond 2.5 mbpd and has not been able to attract investment to spur new refineries, despite past oil booms. Besides, the operations of oil theft and vandals currently constitute a national menace as they are eroding the investments of oil companies. This amounts to a huge disincentive for new and existing investors in Nigeria's oil and gas sector. Consequently, there has been declining investment in the petroleum industry, and we continue to see the exit of International Oil Companies (IOCs). While the energy space is transiting to clean technology and the IOCs are being pressured to reduce their hydrocarbon activities, the oil theft and vandalism, increasing operating cost, loss of oil production, and some regulatory hassles have been discouraging. This has led to shutdowns and discontinuation of operation across many oil wells and contributes substantially to the shortfall in crude oil production in Nigeria.

» **High Cost of Production**

The NESG points out the issues of competitiveness in Nigeria's oil and gas operations. The unit cost of production in Nigeria is very high and is a major factor eroding value derived from crude oil prices. At about \$21 – \$30pb, Nigeria has one of the highest unit costs of production globally. This is a far cry from an average cost of \$8.38pb in Saudi Arabia, \$9.08 in Iran and \$10.57 in Iraq. Essentially, Nigeria will need a very high oil price to maximise the revenue and foreign exchange inflows from crude oil sales. The issue of oil theft and security of oil facilities top the list of factors driving the high cost of production in the sector. Oil companies have to provide their security and devise alternative evacuation systems with higher costs in manifolds than channelling through pipelines.

» **Subsidies Payment**

The NESG notes that the perennial issue of fuel subsidies continues to drain revenue and foreign reserves as the subsidy removal implementation specified in the PIA has been postponed. Nigeria currently exports crude oil while it imports finished petroleum products. However, the recent practice is that the NNPC Limited swaps crude oil for

fuel. Hence, there is a netting off foreign exchange earnings. Besides, the government heavily subsidises the Premium Motor Spirit (PMS) from the already strained oil revenue. For every US\$1 increase in oil price, fuel imports revert about 34 cents while subsidies payment eats up 54 cents of every dollar of oil revenue. As such, a sizable proportion of what is supposed to go to the government's purse ends up as payment for subsidies. With the elevated oil price, the NNPC has already requested N3 trillion for fuel subsidy payments in 2022, which will further compound Nigeria's fiscal distress. Furthermore, subsidised fuel also faces the challenges of oil theft and vandalism. In 2021, an estimated 116.5 million litres of PMS (amounting to about N19 billion) was stolen⁶, which further sabotaged the resources that the government would have retained.



⁶<https://nairametrics.com/2022/03/28/petrol-worth-n18-88-billion-was-stolen-in-2021-in-nigeria-nnpc/?amp=1>

Recommendations

The NESG commends the government for the progress so far with the implementation of the PIA – the Nigerian Upstream Petroleum Regulatory Commission (NUPRC) and the Nigerian Midstream and Downstream Petroleum Regulatory Authority (NMDPRA) are afloat and already setting a footprint for a new era in the oil and gas sector. The NESG, therefore, proposes six (6) point recommendations to forestall the current decline in foreign exchange inflows from oil.

01

First, while the PIA provides an operating guideline in the oil and gas sector, the NESG calls for an integrated strategy and framework for the effective implementation of the PIA, addressing security challenges and attracting investment in the sector. This would be a collaborative effort of the Nigerian Upstream Petroleum Regulatory Commission (NUPRC), the NNPC Limited/Joint Venture and security agencies responsible for pipeline and waterway security.

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03

Third, the NESG recommends that the government must ensure the security and reliability of pipelines and crude oil infrastructure. This requires that the government needs to get the pipelines in good shape, having been damaged by vandals and weakened over time. The government needs to leverage Public-Private Partnerships in providing some of these infrastructures. Also, the security of pipelines is paramount - the government needs to beef up security on the waterways, adopts technology in the surveillance of pipelines and brings the individuals involved in oil theft and vandalism to book.

04

Fourth, the activities of the Niger Delta militant groups do appear subsided. However, members of the militant groups would be complicit in oil theft and vandalisation of pipelines. Hence, the NESG advises, as emphasised in the PIA 2021, that the issue of host community development needs to be taken more seriously. Therefore, the government needs to ensure effectiveness in implementing the Host Community Development provisions of the PIA 2021.

05

Fifth, the NESG encourages the government to promote local content. The exit of IOCs allows the government to encourage local oil companies to take the mantle from foreign investors. Also, local companies being owned by Nigerian citizens could provide room for a better understanding of the terrain and better interaction and management of the restiveness of host communities.

05

Lastly, the NESG notes that the PIA provisions have a strong footprint for the development of gas exploration in Nigeria. The group advises the government to be vigorous with the development of the gas exploration segment of the industry, at least to advance sufficient local consumption.





ABOUT NESG

The NESG is an independent, non-partisan, non-sectarian organization, committed to fostering open and continuous dialogue on Nigeria's economic development. The NESG strives to forge a mutual understanding between leaders of thought so as to explore, discover and support initiatives directed at improving Nigeria's economic policies, institutions, and management.

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