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FREE FLOAT OF THE NAIRA: THE EFFECT ON THE NIGERIAN ECONOMY[1]

1. INTRODUCTION

On the 14th of June 2023, the Central Bank of Nigeria ("CBN") published a press release on the Operational Changes to the Foreign Exchange Market.[2] The information disseminated to the public was to notify it of the abolishment of segmentation, and collapse into the Investors and Exporters (I&E) window. The CBN re-introduced the "willing buyer, willing seller" model at the I&E window. Simply put, the agreed price by the buyer and seller will determine the rate at which the Naira is exchanged for any foreign currency.

The Naira has been subjected to a free float and the exchange rate is no longer decided by the government or the CBN. It implies that the combination of the forces of supply and demand for foreign exchange will determine the exchange rate as opposed to CBN. The float was proposed in 2022, however, it did not come into fruition until now. Several financial analysts have noted that the float could result in the devaluation of the currency, but if appropriate policies and safety nets are put in place, then it might attract foreign investments and economic improvements.

The Naira which was sold at various rates on official and black market is supposedly now the same everywhere. Some financial experts say that the system will allow the

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2 See, Press Release: *Operational Changes to the Foreign Exchange Market*, Central Bank of Nigeria available at https://www.cbn.gov.ng/Out/2023/CCD/Operational%20Changes%20to%20FX%20Market.pdf accessed on 24th July 2023.

Naira to respond to fluctuations in international markets and increase competition by allowing the currency to adjust to shifting economic conditions. While some other experts say that a rise in the volatility of the Naira might have unfavourable effects on the economy.

Floating any country's currency will have both economic benefits and repercussions. In this article, we will look at some probable effects the free float will have on the Nigerian economy.

2. THE EFFECT OF THE FREE FLOAT ON THE NIGERIAN ECONOMY

The free float of the Nigerian economy has had counterintuitive effects so far and we are looking forward to seeing a bright light at the end of the tunnel soon. Some of the effects are as follows:

2.1. Volatility in currency rates

Floating the Naira will cause more volatility in the currency rates. In a system with a floating exchange rate, supply and demand in the market determine how much a currency is worth. Therefore, the value of the Naira will change in reaction to a variety of economic factors, such as interest rates and foreign investment. There may be an upward surge in the economy and increased competition with this volatility.

2.2. Increase in exports

There may be increase in exports as a result of the Naira float. The value of the Naira may decline with the free float, thereby making Nigerian goods for foreign consumers less expensive. This can encourage companies that are focused on exports, boost revenue from foreign exchange, and lessen the nation's dependency on oil exports. It would encourage economic diversification and contribute to the creation of a stronger, more durable economic system.

2.3. Inflation on imports

The increased costs for businesses and consumers may result from a major depreciation in the value of the Naira. This might raise the cost of imported goods and raw materials. Nigeria has always depended on imports, and now with the devaluation, these imports will become more expensive to maintain.

2.4. Foreign debt and financial instability

The foreign debt and financial stability of Nigeria may be impacted by the Naira's float. A lot of these debts are in foreign currency, and the country's debt commitments will

rise when converted if the Naira fell in value. This might make it harder for the government to repay its debts.

2.5. **Decline in investor confidence**

The Naira volatility may trigger a decline in investor confidence, and endanger the stability of the financial system. Any country that hopes to trade in foreign exchange needs to have investors that have confidence in its currency. As a result of this float, any decline in the Naira value will cause investors to lose confidence and refuse to transact with any industry in the country.

3. RECOMMENDATIONS TO CUSHION THE EFFECTS OF THE FREE FLOAT

The effect of the free float of the Naira on the Nigerian economy hinges on finding the right balance between market-driven exchange rate dynamics and proactive government interventions. With prudent management, a free float has the potential to attract foreign investments, boost exports, and contribute to long-term economic growth and stability in Nigeria. Let us look at some specifics below.

3.1. **Inflation on imports and increase in exports**

To control inflation and uphold price stability, the Government would need to undertake efficient monetary policies and measures, such as interest rate changes and stringent fiscal controls. Tariffs should be instituted on foreign imports in order to protect businesses and consumers and promote use of domestic products. Price control regulations and measures should be put in place to prevent hikes due to the devaluation of the Naira. Support and priority should be given to the agricultural industry to increase productivity, reduce imports and increase exports of quality products. The Government should set up policies that would be favourable and promote exports, so as to motivate companies to produce high quality goods for export. This will generate revenue and boost the inflow of foreign exchange to create a more secure economy.

3.2. **Foreign debt and financial instability**

For Nigeria’s debt commitment not to rise, it is necessary policies and measures like plugging revenue leakage and generating additional revenue streams by investing in key sectors of the economy should be put in place. The Government should prioritise job security, skill development programs, entrepreneurship support to enable the people gain financial stability. The richer the people, the richer the economy.

3.3. **Volatility in currency rates and decline in investor confidence**

Measures should be taken to increase the value of naira and reduce naira volatility so as to build investor confidence, encourage economic adjustments and boost competition. When investor's confidence rise in the economy, then more investors will want to transact in various industries in the country.

4. CONCLUSION

Floating the Naira can be interpreted as an indication of economic reform and draw in outside capital. International investors may have more faith in a country's ability to implement market-driven policies if the exchange rate mechanism is flexible.

For a free float of the Naira to have a positive effect on the Nigerian economy, it requires careful monitoring and appropriate policy interventions by the Government and the CBN. Implementing measures to manage exchange rate volatility, promoting export-oriented industries, and encouraging investment in critical sectors can help maximize the benefits while mitigating potential risks.

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