

CENTRE FOR THE PROMOTION OF PRIVATE ENTERPRISE (CPPE)

POLICY BRIEF

IMPLICATIONS OF THE IRAN–U.S.–ISRAEL CONFLICT ON THE NIGERIAN ECONOMY

Introduction

The escalating conflict involving **Iran**, the **United States**, and **Israel** has injected a new wave of geopolitical risk into the global economy. Energy markets are the first transmission channel. Of particular strategic importance is the **Strait of Hormuz**, through which roughly 20 percent of global crude oil supply is transported daily. Any disruption to this corridor has immediate implications for global oil prices, shipping costs, insurance premiums, and supply chains. There is also the output disruption effect, as Middle East countries are major oil producers.

For Nigeria, an oil-dependent economy where crude accounts for over 85 percent of export earnings and about half of government revenue, the implications are significant. The effects will be both positive and adverse, depending on the duration of the conflict and the quality of domestic policy responses.

Oil Price Dynamics: Revenue Upside Amid Production Constraints

Geopolitical tensions in the Middle East historically trigger sharp increases in crude oil prices due to fears of supply disruptions. Even speculative risks around the Strait of Hormuz typically generate price volatility of \$5–\$15 per barrel within short periods.

For Nigeria, every increase in crude oil price translates into additional export earnings and fiscal revenues. The immediate benefits include:

- Higher crude export receipts
- Improved foreign exchange inflows
- Strengthening of external reserves
- Increased FAAC allocations to all tiers of government

However, revenue gains are critically dependent on production levels. Nigeria's current crude output has fluctuated around 1.4–1.6 million barrels per day, below installed capacity and vulnerable to oil theft, pipeline vandalism, and underinvestment in upstream infrastructure. Without a sustained improvement in production efficiency and security, Nigeria may not fully optimise any price windfall.

There is also a medium-term risk. If the conflict escalates and dampens global growth, oil demand could weaken, leading to price corrections. The fiscal upside is therefore inherently fragile.

Exchange Rate Implications and Capital Flow Risks

Higher oil prices typically strengthen Nigeria's current account balance and improve foreign exchange liquidity. This could reduce short-term pressure on the naira and reinforce investor confidence.

In recent years, exchange rate stability has been closely tied to oil receipts and capital inflows. Improved export earnings could:

- Boost gross external reserves
- Enhance FX market liquidity
- Reduce speculative pressure on the currency

However, geopolitical instability also triggers global risk aversion. During periods of uncertainty, capital tends to migrate toward safe-haven assets such as U.S. Treasury securities and gold. Emerging markets frequently experience portfolio outflows in such episodes.

Given Nigeria's relatively shallow capital market and sensitivity to foreign portfolio investment, volatility in global financial conditions could offset part of the FX gains from higher oil prices. The net exchange rate impact will therefore depend on the balance between stronger oil inflows and potential capital reversals.

Inflation Transmission and Welfare Pressures

The most immediate domestic risk lies in inflation transmission.

Nigeria operates a deregulated downstream petroleum regime. Higher international crude prices feed directly into higher petrol, diesel and aviation fuel costs. The likely channels include:

- Rising pump prices
- Increased transportation/logistics costs
- Higher food distribution expenses
- Escalating manufacturing and logistics costs

Energy costs have a strong multiplier effect in Nigeria’s inflation dynamics. Transportation and food prices account for a significant share of consumer expenditure. With purchasing power already fragile, sustained increases in fuel prices could intensify cost-of-living pressures and deepen poverty levels.

Thus, while government revenues may rise, household welfare could deteriorate—creating a divergence between fiscal gains and social outcomes.

Implications for the Capital Market

The Nigerian capital market is likely to experience differentiated sectoral impacts.

Upside

Oil and gas equities may benefit from improved earnings expectations and stronger investor interest in energy-linked assets.

Risks:

Downside

Manufacturing, aviation, logistics, and consumer goods companies may face margin compression due to higher energy and input costs. Foreign portfolio flows could weaken if global financial tightening intensifies.

Risks:

Short-term volatility in equity and fixed-income markets is therefore expected to increase.

Fiscal Management: Fiscal Consolidation Opportunity

Nigeria’s fiscal history demonstrates that oil windfalls often lead to expenditure expansion during price booms, followed by fiscal stress when prices normalize.

The current situation presents an opportunity for disciplined fiscal consolidation. Priority actions should include:

- Saving part of any oil windfall in stabilization mechanisms
- Reducing fiscal deficits
- Moderating public debt accumulation
- Prioritising capital expenditure over recurrent spending

Without prudent management, temporary revenue gains could encourage unsustainable spending patterns, increasing vulnerability when oil prices eventually decline.

Broader Global Growth and Trade Risks

If the conflict broadens:

- Global shipping insurance costs may rise
- Supply chains could face disruptions
- Commodity markets may experience sustained volatility
- Global growth could moderate

Nigeria's mono-product export structure amplifies its exposure to such external shocks. Structural diversification remains imperative.

Policy Recommendations

CPPE recommends the following strategic responses:

1. **Strengthen Oil Production Capacity:** Intensify anti-theft operations and incentivize upstream investment to maximise output within OPEC limits.
2. **Build Fiscal Buffers:** Channel excess revenues into stabilization and sovereign savings frameworks.
3. **Accelerate Refining Capacity:** Deepen domestic refining to reduce vulnerability to imported refined products.
4. **Sustain FX Market Reforms:** Enhance transparency and liquidity in the foreign exchange market to mitigate volatility.
5. **Deploy Targeted Social Protection:** Cushion vulnerable households against energy-driven inflation shocks.
6. **Fast-Track Economic Diversification:** Expand non-oil exports, manufacturing, agro-processing, ICT, and services to reduce external vulnerability.

Conclusion

The Iran–U.S.–Israel conflict represents a classic double-edged shock for Nigeria. Higher oil prices may strengthen fiscal and external balances in the short term. However, inflationary pressures, welfare deterioration, capital flow volatility, and global growth risks pose significant countervailing threats.

The ultimate impact will depend less on external events and more on domestic policy discipline. Strategic savings, production efficiency, macroeconomic prudence, and structural diversification will determine whether Nigeria converts geopolitical turbulence into macroeconomic resilience.

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