THE NIGERIAN ECONOMIC SUMMIT GROUP

Boom Not Gloom

Nigeria's Optimal Policy Response to the US/Israel–Iran War

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INTRODUCTION

The escalation of tensions between the United States, Israel, and Iran in late February 2026 has triggered the most significant global energy shock since the Russia–Ukraine war. For Nigeria, the implications are mixed. Higher global oil prices could generate a substantial fiscal windfall and strengthen foreign exchange (FX) inflows. At the same time, rising global energy prices may translate into domestic inflation through higher fuel and logistics costs.

Nigeria's geographic position as an Atlantic crude exporter provides a degree of insulation from disruptions in the Strait of Hormuz, one of the world's most critical energy chokepoints. This means Nigeria can benefit from higher oil prices without facing the direct supply disruptions experienced by Gulf producers.

Under plausible scenarios, Nigeria could record additional oil revenues ranging from about ₦2.3 trillion under a short-lived shock to as much as ₦30 trillion if the conflict becomes prolonged. However, the upside is not guaranteed. Structural constraints in the oil sector, inflationary pressures from higher energy prices, and election-cycle spending pressures could limit the benefits if policy responses are poorly calibrated.

This policy brief argues that Nigeria can convert the crisis into an opportunity to strengthen macroeconomic stability if policymakers respond with discipline. The recommended strategy is straightforward: save the windfall, maintain monetary discipline, strengthen external buffers, and protect vulnerable households through targeted support rather than broad price controls.

If carefully managed, the crisis could consolidate Nigeria's recent reform progress. Conversely, a weak policy response risks repeating the country's historical boom-bust pattern, where oil windfalls translate into rapid spending expansions that erode fiscal discipline and destabilise the macroeconomy.

2.0 The Global Shock: What Happened

On 28 February 2026, coordinated military strikes by the United States and Israel on Iranian strategic infrastructure triggered retaliatory attacks across the Gulf region. The escalation injected significant geopolitical risk into global oil markets, pushing prices sharply above pre-crisis levels. The Strait of Hormuz, through which roughly one-fifth of global oil supply passes, sits at the centre of these tensions. Disruptions to shipping through this narrow corridor immediately affect global energy markets.

Nigeria, however, is structurally insulated from this chokepoint. As an Atlantic exporter, Nigerian crude shipments depart from terminals along the Gulf of Guinea and reach global markets without transiting Hormuz. This geographic advantage allows Nigeria to benefit from higher global oil prices even when Gulf supply routes are disrupted.

To assess the potential macroeconomic implications of the crisis for Nigeria, we consider three stylised oil price scenarios:

Table 1. Oil Price Scenarios Used in the Policy Analysis

Scenario	Duration	Description	Oil Price (US$/bbl)	Average Price (US$/bbl)	Note
S1: Short-lived, Contained Crisis	4–6 weeks	Conflict remains militarily contained; temporary disruption of Strait of Hormuz, quickly restored.	80–100	90	Base case; held by most professional forecasters
S2: Prolonged Regional Crisis	Up to 3 months	Conflict spreads to other Gulf states, severely disrupting tanker traffic and raising insurance costs.	100–120	110	Most probable near-term path; futures and forward prices leaning toward this scenario
S3: Protracted Global-Scale Crisis	Up to 6 months	Crisis escalates globally, causing protracted supply disruptions, sanctions, trade barriers, and risk of recession.	120–140	130	Worst-case scenario; tail risk at $140

The macroeconomic implications for Nigeria differ across these scenarios, but the direction of impact remains broadly similar: higher oil revenues alongside inflationary pressures from global energy prices.

3.0 Tracing the Transmission Channels to Nigeria

The Middle East crisis could transmit both opportunities and risks to the Nigerian economy through several macroeconomic channels. On the positive side, higher global oil prices could boost fiscal revenues and improve foreign exchange inflows. On the downside, the shock could raise imported inflation, trigger capital outflows during global risk-off episodes, and increase production costs for key sectors such as manufacturing and agriculture.

The net macroeconomic outcome will therefore depend on which forces dominate and how policymakers respond. To quantify these trade-offs, this analysis combines fiscal accounting techniques with a calibrated semi-structural New Keynesian open-economy model of the Nigerian economy to estimate the macroeconomic implications under three plausible crisis scenarios.

3.1 The Fiscal Windfall Channel

Nigeria stands to benefit from a significant fiscal windfall as oil prices rise well above the 2026 budget benchmark of US$64.9 per barrel. The budget also assumes production of 1.84 million barrels per day and an exchange rate of ₦1,400 per US dollar.

Under a short-lived crisis scenario (S1) lasting five weeks with oil prices averaging US$90 per barrel, Nigeria could earn about US$1.62 billion (₦2.27 trillion) in additional oil revenue above the budget benchmark.

Using the RMAFC revenue-sharing formula, this would translate to roughly ₦1.19 trillion for the Federal Government and ₦1.07 trillion for states and local governments through FAAC, equivalent to about one month of federal debt-service obligations.

If the crisis escalates into a regional conflict (S2) with oil prices averaging US$110 per barrel for three months, the windfall could rise to US$7.48 billion (₦10.47 trillion). The Federal Government's share of about ₦5.51 trillion would be sufficient to finance roughly one-fifth of the 2026 capital expenditure budget.

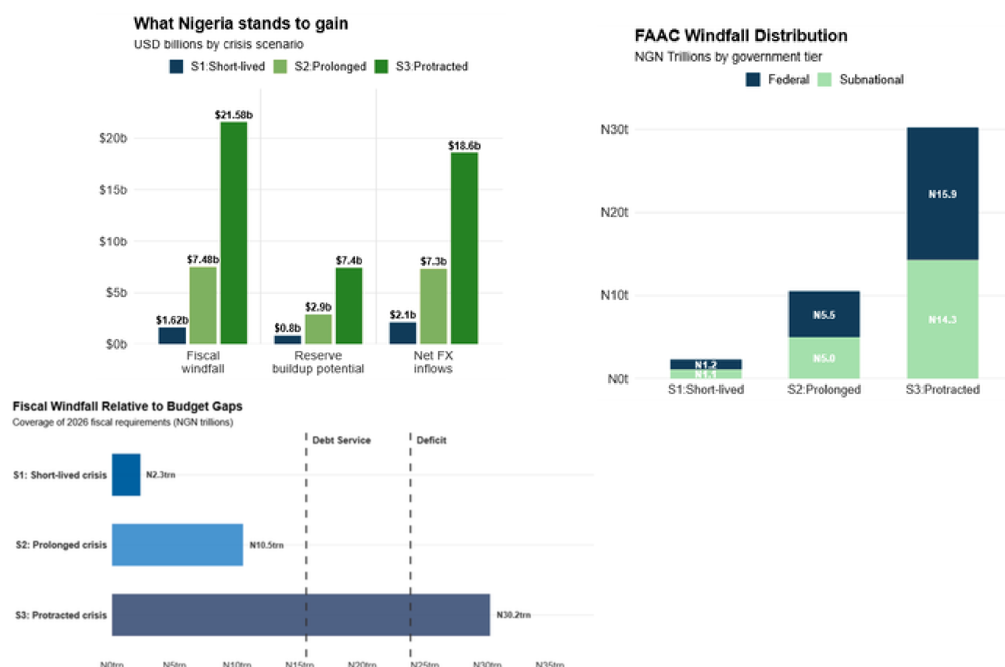
Under a severe global escalation scenario (S3) with oil prices averaging US$130 per barrel for six months, the windfall could reach US$21.58 billion (₦30.21 trillion). The Federal Government's share alone, around ₦15.91 trillion, would be large enough to cover all federal debt-service obligations or about 60 percent of the capital budget.

These estimates should, however, be treated cautiously. Oil production remains below budget assumptions. In the first quarter of 2026, output averaged about 1.48 million barrels per day (see OPEC, 2026; NUPRC, 2026), well below the 1.84 million barrels per day budget assumption. Adjusting for this gap would reduce the projected windfall by roughly 20 percent, highlighting the cost of persistent production constraints. Also, security challenges, infrastructure leakages, and crude oil theft continue to limit Nigeria's ability to increase production quickly.

On the positive side, full implementation of Executive Order No. 9 of 2026, which mandates the direct remittance of oil and gas revenues into the Federation Account, could improve fiscal transparency and ensure that windfall revenues flow through FAAC rather than being retained at source.

Importantly, Nigeria now enters this crisis without the fuel subsidy regime, which previously absorbed much of the benefit from higher oil prices. Under the old system, a shock of this magnitude could have generated an additional ₦2–₦5 trillion subsidy bill, largely offsetting the fiscal gains.

Fig 1 Crude Oil Price Paths Under Alternative Conflict Scenarios



Notes: Higher oil prices could generate sizeable fiscal windfalls, strengthen foreign exchange inflows, and provide additional fiscal space relative to key budget gaps. Under the most severe scenario, the windfall could exceed ₦30 trillion, with the Federal Government's share alone large enough to cover annual debt-service obligations and significantly expand reserve buffers.

Resisting Pro-Cyclical Windfall Spending

The perceived fiscal windfall, combined with the approaching election cycle, may generate pressure from subnational governments, legislators, and organised groups for higher spending and short-term palliative measures.

Managing these pressures without reversing recent reforms will be a key test of fiscal discipline and policy credibility. In particular, calls to reintroduce fuel subsidies as a response to rising transport and food costs should be resisted, as this would risk reinstating the fiscal distortions that recent reforms sought to eliminate.

3.2 The Imported Inflation Channel

Nigeria has historically faced the "oil-exporter–refined-product-importer paradox", where higher global oil prices simultaneously increased export revenues and raised the cost of imported refined petroleum products. Under the former subsidy regime, domestic fuel prices were artificially suppressed, insulating consumers from global price shocks but creating large fiscal liabilities.

Following the removal of the subsidy and the shift towards market-based fuel pricing, global oil price increases now transmit more directly to domestic pump prices. Higher fuel prices raise transportation and logistics costs, feeding into broader consumer price inflation.

However, this transmission is now partly mitigated by domestic refining capacity, particularly the Dangote Refinery, which has significantly reduced Nigeria's reliance on imported refined products. Recent downstream data indicate that in January 2026, domestic refineries, driven largely by Dangote, supplied approximately 40.1 million litres per day of PMS, representing about 62 percent of total national supply, while average consumption stood at around 60.2 million litres per day.

The shift towards domestic refining reduces Nigeria's exposure to shipping costs, insurance premiums, and supply disruptions that typically accompany geopolitical crises. Nevertheless, the buffer is partial rather than complete, as domestic fuel prices remain linked to international crude oil benchmarks.

Risks to Disinflation

The oil price shock could temporarily slow Nigeria's ongoing disinflation process. However, two factors help moderate the inflationary impact.

First, domestic refining capacity reduces reliance on imported refined products, lowering the exposure to global refined-product price spikes. Second, higher oil revenues could improve foreign exchange liquidity, potentially strengthen the naira and lower the FX component of domestic fuel prices.

Even with these buffers, the inflation pass-through remains significant. Model simulations suggest that the oil price shock could add between 1.3 and 5.2 percentage points to headline inflation over the next two to three quarters, depending on the crisis scenario.

- Under S1 (US$90 per barrel), inflation increases by about 1.3 percentage points.

- Under S2 (US$110 per barrel), inflation rises by roughly 2.9 percentage points.
- Under S3 (US$130 per barrel), inflation could increase by around 5.2 percentage points due to stronger second-round effects.

Without the buffering effect of domestic refining, the inflation impact would have been substantially larger, estimated at 3.1, 7.2, and 12.8 percentage points under the three scenarios respectively. In effect, the Dangote Refinery could help avoid between 1.8 and 7.6 percentage points of additional inflation.
Encouragingly, model results suggest that inflation eventually returns to its pre-crisis disinflation path under all scenarios, provided monetary policy remains appropriately calibrated and does not accommodate the temporary cost-push shock. In this sense, the crisis may delay—but not derail—Nigeria's disinflation trajectory.

3.3 Exchange Rate and External Reserves

Higher oil prices create a dual shock to the naira. On one hand, stronger oil export revenues boost foreign exchange inflows and support the current account. On the other hand, higher import costs and potential risk-off capital outflows during a prolonged crisis could weaken the currency.

Under the short-lived (S1) and regional crisis (S2) scenarios, the positive FX channel is likely to dominate. Additional FX inflows are estimated at US$2.1 billion under S1 and US$7.3 billion under S2, largely from oil export receipts above the budget benchmark. With the pre-crisis NAFEM rate around ₦1,300–₦1,400 per US dollar, sustained inflows could push the naira towards ₦1,200–₦1,300 per US dollar. This appreciation would be disinflationary, reducing the naira cost of imports and partially offsetting the inflationary impact of higher global oil prices.

Nigeria's large interest-rate differential, at over 20 percentage points above US rates, could also sustain portfolio inflows into domestic money-market instruments, provided global financial conditions remain stable. This would allow the Central Bank of Nigeria (CBN) to further strengthen external buffers. With gross reserves at US$50.45 billion as of mid-February 2026, the CBN could add about US$0.8 billion under S1 and US$2.9 billion under S2, assuming roughly 40 percent of additional inflows are accumulated into reserves.

Under the severe global crisis scenario (S3), however, the balance could shift. Although oil FX inflows could reach US$21.6 billion, heightened global risk aversion could trigger portfolio outflows of US$3 billion or more, widening sovereign spreads and weakening investor sentiment. The naira could initially appreciate before facing renewed depreciation pressures as capital flows reverse.

Even in this scenario, net FX inflows could still reach about US$18.6 billion, enabling the CBN to increase reserves by up to US$7.4 billion, potentially lifting gross reserves above US$57 billion.

Overall, the exchange-rate channel is supportive of naira appreciation and reserve accumulation under contained crisis scenarios, but becomes more uncertain under a prolonged global shock. The appropriate policy response is to allow the exchange rate to adjust to fundamentals, intervene only to smooth excessive volatility, and opportunistically build reserves during periods of strong oil inflows.

4.0 Optimal Policy Response

The Middle East crisis presents Nigeria with both risks and opportunities. Policymakers face a narrow window to safeguard the macroeconomic stability achieved through recent reforms while ensuring that temporary oil windfalls do not trigger a return to the country's familiar boom–bust cycle. The overarching policy objective should therefore be to convert the crisis into an opportunity while consolidating hard-won reform gains.

4.1 Fiscal Policy Response

Historically, oil windfalls have weakened fiscal discipline in Nigeria, particularly during politically sensitive periods. Without clear safeguards, higher oil revenues could trigger pro-cyclical spending and policy reversals. To avoid this outcome, the fiscal response should be rules-based rather than discretionary, anchored on the following actions:

I. Enforce full remittance of oil revenues: The government should fully implement Executive Order No. 9 (2026), which mandates the direct remittance of all oil and gas revenues into the Federation Account. By eliminating discretionary retention of revenues by NNPC Ltd., the order strengthens fiscal transparency and ensures that oil windfalls are subject to legislative oversight and the statutory sharing formula. Strict implementation will prevent off-budget spending and reinforce recent governance reforms.

II. Save windfall revenues above the budget benchmark: Fiscal authorities should resist pressures to expand spending through supplementary budgets. Instead, revenues above the 2026 benchmark oil price of US$64.9 per barrel should be automatically saved in the stabilisation framework, such as through the Nigeria Sovereign Investment Authority (NSIA) or a designated stabilisation account. These resources can subsequently be appropriated for clearly defined priority investments through established fiscal processes.

III. Use part of the windfall to reduce public debt: A portion of the additional oil revenue should be allocated to retiring expensive short-term domestic debt. Nigeria's interest payments, estimated at ₦15.52 trillion in 2026, consume nearly half of projected federal revenues. Debt reduction would ease fiscal pressures, reduce crowding-out of private investment, and strengthen monetary policy effectiveness.

IV. Maintain the fuel subsidy reform: The removal of the petrol subsidy should remain firmly in place. Reintroducing subsidies in response to rising global oil prices would recreate fiscal distortions and erode recent reform gains. Analysis suggests that maintaining the old subsidy regime during the crisis would have generated additional fiscal costs of ₦2–₦5 trillion, largely offsetting the oil windfall.

V. Expand targeted social protection: Rather than suppressing prices administratively, the government should temporarily expand targeted cash transfers to protect vulnerable households from higher transport and energy costs. Scaling the National Social Safety Net Programme to cover up to 15 million households would provide more effective and fiscally efficient protection than blanket fuel subsidies.

4.2 Monetary Policy Response

The key challenge for monetary policy is to preserve the ongoing disinflation process while managing temporary supply-side inflation pressures arising from higher global oil prices. Model estimates suggest that inflation will eventually return to the pre-crisis disinflation path, provided monetary policy remains disciplined and credible. The optimal response includes the following measures:

I. Maintain a data-driven monetary policy stance: Because the shock is largely supply-driven, the Central Bank should avoid premature policy tightening. A cautious "wait-and-see" approach, maintaining the current policy stance while closely monitoring inflation dynamics, would prevent unnecessary harm to economic growth.

II. Provide clear forward guidance: The Central Bank should communicate transparent scenario-based guidance explaining how monetary policy would respond under alternative oil price outcomes. Such communication would anchor expectations, reassure financial markets, and reinforce the credibility of the disinflation strategy.

III. Sterilise excess liquidity from oil revenues: Higher oil exports will generate additional foreign exchange inflows and increase naira liquidity through FAAC distributions. The Central Bank should sterilise these inflows through open market operations and targeted liquidity management to prevent monetary expansion from fuelling inflation.

IV. Allow exchange rate flexibility: The exchange rate should be allowed to adjust to improved oil-driven foreign exchange inflows, with interventions limited to preventing disorderly market conditions. Currency appreciation, where warranted by fundamentals, would help moderate imported inflation.

V. Strengthen external reserves: Elevated oil prices provide an opportunity to rebuild external buffers. The Central Bank should opportunistically accumulate foreign exchange reserves from the windfall inflows, further strengthening Nigeria's external resilience against future shocks.

5.0 Conclusion: Do Not Let the Crisis Go to Waste

The US/Israel–Iran conflict presents Nigeria with a time-limited opportunity to turn an external shock into a consolidation of hard-won macroeconomic stability. Fiscal windfalls could range from ₦2.3 trillion under a short-lived crisis to ₦30.2 trillion under a protracted scenario, with headline inflation temporarily rising 1.3–5.2 percentage points and the naira benefiting from oil FX inflows.

Nigeria's response should focus on three priorities:

- **Save the windfall.** Full implementation of the President's Executive Order on oil revenue remittance is essential to ensure transparency, prevent off-budget spending, and preserve fiscal discipline.
- **Hold the monetary line.** The CBN should avoid reactive tightening to transitory supply shocks, sterilise excess liquidity, and allow the naira to adjust to market fundamentals.
- **Communicate proactively.** Credible, scenario-based forward guidance from both fiscal and monetary authorities is critical to anchor expectations and reduce self-fulfilling market disturbances.

The January 2027 election cycle is the key domestic risk, testing political will to ring-fence windfalls, resist pro-cyclical spending, and sustain non-oil fiscal reforms.

Finally, while the situation remains fluid, policymakers should maintain a high frequency monitoring dashboard focused on five key indicators: (i) Brent crude prices and tanker traffic on the Strait of Hormuz, as a gauge of conflict duration and scenario selection; (ii) Nigeria's crude oil production levels, as the reality check for actual output; (iii) the naira NAFEM rate, as an early warning of FX stress or capital flow reversal; (iv) CPI food and transport sub-indices, as signals of second-round inflation pass through that would warrant monetary policy reassessment; and (v) developments in Nigeria's financial account, as early indicators of portfolio capital flow sentiment.

Summary of Policy Response Matrix

Policy Action	Rationale / Quantitative Support	Timeline
FISCAL POLICY PACKAGE		
Fully implement Executive Order No. 9 on oil-revenue remittance to FAAC	Ensures the oil windfall actually reaches the Federation Account rather than being retained at source by NNPC Ltd, as occurred in prior oil-price cycles. Provides the institutional anchor for all other fiscal actions.	Immediate
Ring-fence and save the windfall above the $64.85/bbl budget benchmark	Prevents ad hoc supplementary budgets that absorb the windfall into recurrent spending. Revenues above benchmark should be saved in NSIA or a stabilisation account and appropriated ex post for defined priority projects.	Immediate
Use part of the windfall to retire expensive short-term domestic debt	Debt service currently absorbs nearly half of total budgeted revenue, crowding out capital spending and reinforcing fiscal dominance of monetary policy. Retiring high-cost domestic debt creates immediate fiscal space and supports monetary transmission.	Within 30 days
Firmly resist any pressure to reintroduce fuel subsidies	The Dangote Refinery now provides a buffer against global fuel-price shocks. Reintroducing subsidies would reverse reform progress and recreate the perverse fiscal distortion.	Ongoing
Scale targeted cash transfers to vulnerable households	Higher energy and transport costs disproportionately affect low-income households. Expanding the National Social Safety Net Programme is more effective and better targeted than blanket price suppression through subsidies.	Within 60 days
MONETARY POLICY		
Hold the MPR at the current level; do not tighten reactively	The inflation impulse from higher global oil prices is primarily supply-side and transitory. Monetary tightening is an aggregate-demand tool and cannot address supply-driven cost-push inflation.	Next 2 MPC meetings, depending on incoming data
Issue explicit, scenario-based forward guidance	Proactively communicate how monetary policy will respond under alternative oil-price paths. Clarify that the initial impulse is viewed as transitory, while signaling readiness to tighten decisively if second-round demand-pull effects emerge and prove persistent. Reduces market uncertainty and anchors inflation expectations.	Immediate
Sterilise oil-driven naira liquidity surges	Higher oil revenues flowing through FAAC will inject substantial naira liquidity as the CBN purchases FX inflows. Without sterilisation, this translates into unintended monetary expansion that could stoke demand-side inflation on top of the cost-push impulse. Use OMO and targeted CRR adjustments.	Ongoing
Allow the naira to appreciate on the back of oil-FX inflows	Naira appreciation from oil-export receipts is itself disinflationary, compressing the naira cost of imported goods and fuel, and partially offsetting the cost-push inflation channel. Intervene only to smooth disorderly volatility, not to defend a specific level.	Ongoing
Opportunistically build external reserves with the FX windfall	Though gross reserves are at 13-year high, net reserves remain vulnerable, leaving the country exposed to sudden FX shocks. The oil windfall provides a rare opportunity to accelerate reserve buildup.	Ongoing
RISK MANAGEMENT		
Resist pro-cyclical election-cycle spending pressure	January 2027 election is the single largest endogenous tail risk. Political will to ring-fence the windfall and sustain non-oil fiscal reforms through the electoral period is the decisive litmus test.	2026–2027
Maintain a high-frequency monitoring dashboard	Track five key indicators weekly: (i) Brent crude and Hormuz traffic signals, (ii) Nigeria crude production levels, (iii) Naira NAFEM rate, (iv) CPI food and transport sub-indices for second-round pass-through, and (v) Financial account flows for portfolio capital reversal.	Weekly

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The NESG is an independent, non-partisan, non-sectarian organisation, 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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