Exchange Rate Policy and Economic Management: A Theoretical Nexus

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I. Introduction

The basic objectives of economic management are centered on ensuring economic prosperity for the greatest majority of the citizenry with sustainable external balance. This is often associated with significant expansion in the level of economic activities (growth in national output); reduction in unemployment; improved income distribution; significant improvement in the technology of production and its widespread diffusion in the society; improved access to modern and quality education and health care; stable external balance indicators, among others.

Economic management involves formulating and implementing economic strategies and policies that would ensure continuous economic prosperity (internal balance) and sustainable external balance. The first choice in economic management is between market-based economic system and an economic system based on administrative controls. In between the two polar ends are varied degrees of market-based economic systems. With the collapse of the Soviet Union in the 1990s, there appears to be a *de facto* consensus that market-based economic system is the inevitable choice for all.

Among the set of economic policies that are in the tool box of economic managers are exchange rate policies, tariff, exchange and administrative controls; and fiscal and monetary policies. Economic management, therefore, involves the use of exchange rate policies, tariff, exchange and administrative controls, fiscal and monetary policies. An economy that is overall market-based may choose an exchange rate policy that is not market based. Thus, the choice of the exchange rate policy could be made independent of the type of the mode of production and distribution chosen.

It is generally believed that an exchange rate is an important variable that has a significant impact on the overall outcome of macro-economic performance as it concerns internal and external balances. First, it is an important variable because of its impact on aggregate demand. Second, it is an important allocator of resources between the traded and non-traded sectors of the economy. Third, it is also an important variable that wealth holders consider in the allocation of their wealth between investment in physical assets and monetary assets and further among different categories of monetary

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assets. Fourth, it is generally believed to be an important determinant of the general price level, especially in an open economy where consumers have imports as a significant component of their consumption basket. It is for these, and other related reasons that the exchange rate is viewed as an important economic variable and is of importance to governments and monetary authorities the world over.

Furthermore, while an exchange rate change constitutes an expenditure-switching policy, a change in either fiscal or/and monetary policy stance is an expenditure-changing policy. To a limited extent, tariff is an expenditure-switching; limited because of the administrative discretion involved in its implementation.

Nigeria had witnessed a number of economic adversities and has a record of implementing different strands of exchange rate policies with varied outcomes. It is therefore desirable to examine this rich experience to determine how successful its exchange rate policy experience had been with an eye on the future. The objective of the current effort is to examine the record of the Nigerian exchange rate policies in the context of the prevailing conventional wisdom on the subject matter. Specifically, the current effort aims at determining the prevailing conventional wisdom over the period under review and comparing this with Nigerian exchange rate policy records to draw some lessons.

Towards this end, Section 2 discusses the conventional wisdom on the optimal exchange rate regime; Section 3 discusses the Nigerian experience, while Section 4 concludes the current effort.

II. Exchange Rate Regimes

The choice and formulation of exchange rate policies are often discussed and evaluated in the context of the alternative exchange rate regimes from which a choice could be made. In the continuum of conceptually possible exchange rate regimes from which a choice is to be made are the polar cases of flexible (floating) and the fixed exchange rate regimes. In between these two polar cases, you have the managed (or dirty) float closer to floating rate and the crawling peg closer to the fixed rate. Also, it is conceivable to have a multiple-tier exchange rate regime with the limiting case being the dual exchange rate regime like the well-known second-tier exchange rate regime that was practiced in Nigeria in 1986.

In real life, hardly do we see either of the two polar cases in its pure form rather real world exchange rate regimes are classified in accordance with their degrees of exchange rate flexibility. Thus, we hear of fixed rate and more flexible exchange rate regimes as the alternative empirical counterparts of the polar cases.

II.1 The Choice of Exchange Rate Regime

The major case often made for fixed rate is that it promotes international trade and investments and allocative efficiency. Furthermore, it is said that it disciplines monetary authorities to pursue sound monetary policies and it avoids competitive devaluation among countries, thereby promoting orderly foreign exchange market transactions.

On the other hand, flexible rate, being governed by market forces, is said to ensure external balance always and consequently, promotes competitive drives that result in larger national output. It is also said to contain in-built mechanisms via the activities of private speculators, by ensuring that short-run exchange rates are smoothened to their long-run (desirable) levels. Furthermore, flexible rates make exchange rate adjustments less of political decision unlike under fixed rate. Similarly, floating rates are said to perform shock-absorber role as it is said to insulate the domestic economy from external shocks.

The view that stable rates promote international trade and investment and allocative efficiency has been around for a while. For instance, Tower and Willett (1976: 6) quoting Johnson (1970) wrote:

> "... a common money simplifies the profit maximising computations of producers and traders, facilitates competition among producers located in different parts of the country and promotes the integration of markets including both the markets for products and markets for the factors of production (Capital and Labour)."

An application of Johnson's (1970) logic to international trade implies that stable rates would simplify profit-maximising computations and facilitate competition among producers and traders located in different countries thereby promoting efficient allocation in of the world resources. This perhaps lies behind Tower and Willet's (1976) argument that fixed exchange rates would eliminate uncertainty thereby promoting growth of larger and more efficient markets in capital, goods and services, and free resources that would otherwise be engaged in currency conversions thereby raising the level of real income. Similarly, the view that stable rates promote discipline in the use of stabilisation policies and promote orderliness in the foreign exchange market was upheld by the International Monetary Fund (IMF, 1970).

But as early as the 1960s, it was increasingly felt that economies differ in their structural characteristics and that the adoption of either flexible exchange rate regime (FLER) or fixed exchange rate regime (FXER) is with some costs and benefits (Mundell, 1961; Purvis, 1979; Sachs, 1980; Martson, 1982; Harkness, 1982; etc.).

The view that the optimality of the alternative exchange rate market depends on the structural characteristics of the economies concerned has received serious attention since the introduction of the concept of "optimum currency area" by Mundell (1961). Mundell's (1961) principal contribution was to identify factor mobility (especially labour mobility) as

the single factor that determines the optimality of a currency area. Mundell (1961) suggested fixed rates between two countries with high labour mobility. The reason for this view is that if labour is highly mobile between the countries concerned, then, exchange rate changes, as an instrument for righting balance-of-payment disequilibrium would be unnecessary since labour can always move from the deficit region to surplus region, bringing about the required fall in money income in the deficit country relatively to that of the surplus region.

Researches along the line of Mundell (1961) have identified other important factors in the determination of the optimal exchange rate regime. These factors are: wage and price indexing process; source of disturbances; net foreign currency-denominated asset positions; degree of openness; diversification and financial and fiscal institutional set up (Johnson, 1970; Purvis, 1979; Sachs, 1980; Martson, 1982; Harkess, 1982; Jimoh, 1984; Tower and Willett, 1976; Corden 1972; etc). Let us examine these factors in their turns.

II.1.1 Openness and Diversification

Some writers have emphasised the level of economic diversification, the degree of openness and the size of domestic economy as the most relevant factors in the selection of the optimal exchange rate regime. Notable authors of this tradition are Kenen (1969), Johnson (1970) and Purvis (1979).

The main thesis here is that a small economy cannot diversify its production in the presence of economies of scale because it would be costly to do so, but by human nature, consumption is necessarily diversified and diversified consumption with undiversified production implies that a small economy would be highly "open". In such an open economy, a large proportion of domestic income would be spent on foreign products; stabilising the value of domestic currency requires a stable exchange rate, since small changes in exchange rate would effect significant changes in the domestic real income and the value of domestic currency. However, a reasonably stable value of money is generally presumed to be a policy objective since that ensures that money would perform its roles satisfactorily. Hence, for small, open and undiversified economy, the fixed exchange rate regime would be optimal. This was perhaps the rationale behind Johnson's (1970: 97-98) suggestion when he wrote:

> "One is accustomed to thinking of national monies in terms of the currencies of the major countries, which currencies derive their usefulness from the great diversity of goods, services, and assets they can be directly converted. But in the contemporary world, there are many small and relatively narrowly specialised countries whose national currencies lack usefulness in this sense, but instead derive their usefulness from their rigid convertibility at a fixed price into the currency of some major countries with which the small country trades extensively or on which it depends for capital investment. For such countries, the advantages of rigid convertibility in giving the currency usefulness and facilitating international trade and

> investment out-weigh the relatively small advantages that might be derived from exchange rate flexibility. In a banana republic, for example, the currency will be more useful if it is stable in terms of command over foreign goods than if it was stable in terms of command over bananas; and exchange rate flexibility would give little scope for autonomous domestic policy."

Johnson's (1970) comments quoted above, seem to presume that there is money illusion among the residents of the domestic economy. These residents should be concerned with the purchasing power of the domestic currency held and not just with the rigid convertibility of the domestic currency into a key currency. Stability of the purchasing power of the domestic currency is only achieved, in face of exchange rate peg, if foreign prices of major trading partners are stable. When exchange rates fluctuate to reflect the relative strength of currencies due perhaps to different rates of inflation the domestic residents should be indifferent in absence of money illusion.

If one considers the possibility that foreign prices may fluctuate and even widely, then, there is wisdom in Diaz-Alejandro's (1975: 13) statement that:

> "Those arguing that less developed countries should, for their own good, lock their monetary tools with a species of chastity belt and throw away the key appear to assume a relatively tranquil world environment, offering and anchor of price-level stability. Such a view was valid for the late 1950s, and early 1960s, but certainly did not apply during the 1930s and early 1940s and is debatable for the 1970."

Indeed, Diaz-Alejandro's (1975) observation on prices is perhaps valid for today.

II.1.2 Sources of Economic Disturbances

Stein (1963), Black (1976) and Tower and Willet (1976), listed the origin of economic disturbances as relevant factors in the determination of the optimal exchange rate regime. In the words of Tower and Willet (1976):

> "It is rather widely accepted that a country has the strongest case for freely floating exchange rates when the disturbances to its balance of payments typically come from outside its borders and the weakest case when they come from inside".

The reason for this view, as Black (1976) demonstrated, is that FLER is generally believed to insulate an economy from foreign disturbances, while FXER allows an economy to export some of the effects of disturbances of domestic origin. Consequently, FXER would result in smaller variation in prices and output in response to domestic disturbances. Hence, if the above argument is true, an economy experiencing foreign disturbances most of the time should adopt a FLER, otherwise, it should operate a FXER.

However, since the early 1980s, the insulation property of the flexible exchange rates has been questioned by Purvis (1979), Jimoh (1984), and Martson (1982). The central thesis is

that if wages and prices are responsive to changes in exchange rate due to wage indexation and the significant use of imported input in the production process and there is significant net position in foreign currency denominated assets, then FLER has a slim chance of being partially insulating and could possibly be shock exacerbating. Hence, the "Shock-absorber" power of the FLER is more certain when domestic wages and prices are not indexed to foreign prices and the economy has no significant net asset position in foreign currency denominated assets.

In the Nigerian circumstances, it seems that the shocks to external balance originate predominantly in foreign economies, but import-substitution industrialisation ensures that there is a significant level of imported input in the industrial production process, hence, supply prices of industrial products are expected to be highly indexed to foreign prices and exchange rates. This suggests that insulation property of a FLER would be in doubt in Nigeria.

II.1.3 Institutional Set Up

Some authors have identified the financial and fiscal institutions setting as factors relevant to the determination of the optimal foreign exchange market (Lewis, 1979; Black, 1976 and Mundell, 1961). It is generally believed that when the instruments of monetary policy are fragile due to fragmented and underdeveloped nature of money markets and forward markets are non-existent, then the fixed rates would be optimal. Also when the size of the foreign exchange market is thin, a floating exchange rate might not be recommended.

For instance, Lewis (1979: 18-19) listed four reasons why the less developed countries (LDCs) were advised to operate stable rates; and these reasons included the non-existence of forward markets and the fragility of monetary instruments in the LDCs. The fragility of monetary instruments in the LDCs is a tenable reason for recommending the FXER, while the non-existence of forward markets may not be an equally good reason. This is because it is generally believed (especially since the pioneering works of Mundell, 1963; Fleming, 1962; Krueger, 1965; and Sohmen, 1967) that the potency of the monetary policies is higher under floating rates than under fixed while the opposite is the case with fiscal policies (Tower and Willett, 1976: 21). If instruments of monetary policy are fragile in the LDCs, as is generally believed, then an adoption of FLER would imply that only the fragile monetary instruments are available for stabilisation purposes since fiscal policies would be less effective; and they will be better advised to stay on stable rates. But if forward markets are essential for the efficient operation of FLER, and they are so recognised, then, a LDC that wants to adopt a FLER would only have to weigh the costs of establishing the required forward markets against the benefits expected from the operation of FLER. This is because while it might take some efforts to establish forward markets, it would take much more efforts to develop and integrate the fragmented and under-developed money markets in the LDCs. Furthermore, Mundell (1961), Tower and Willett (1976) and others have identified, the size of the foreign exchange markets as a relevant factor to the determination of optimal exchange rate regime. For instance, Tower and Willett (1976: 7) (4) said:

> "...exchange market for currency of a small country might be so thin that a small number of speculators could affect the market price (of foreign currencies under floating rates), increasing the potential for large fluctuations in the external value of the currency ...fostering exchange rate instability..."

This is generally believed and we are not in doubt that in situations where the foreign exchange market is thin, extra measures might be needed to regulate the activities of speculators but this does not entirely rule out the adoption of the FLER in a small country. Hence, the underdeveloped nature of financial markets in the LDCs is more of a relevant factor than the size of foreign exchange markets and the non-existence of forward markets.

The Nigerian financial market could be said to be shallow, fragile and fragmented until the early 1970s, while the same could not be said of it since 1980s. As we have shown elsewhere, empirical evidence suggested that by late 1970's demand for money in Nigeria has become significantly interest-rate sensitive suggesting that its financial market was maturing and monetary policy was becoming effective (Jimoh, 1990: 102).

II.1.4 Net Foreign-Currency Denominated Assets

Purvis (1979), Jimoh (1984), Boyer (1978), Marion (1981) and others have emphasised the role of "wealth effects" of exchange rate changes in the determination of optimal exchange market. In Purvis (1979) and Jimoh (1984), the incorporation of "Wealth effects" ensured that an equal, but opposite change in foreign prices and exchange rates is not neutral. Hence, changes in foreign prices and exchange rates have no equal effects on the domestic economy, resulting in a less favourable result for the insulations properties of the FLER.

The incorporation of "wealth effects" in Boyer (1978) ensured that money market equilibrium conditions were not independent of the exchange rate level if the country had a non-zero net position in foreign currency-denominated assets. This is because changes in the exchange rate result in capital gains or losses thereby changing the size of total wealth. The result is that the domestic economy is integrated to the rest of the world through the foreign exchange cum money markets. This narrows down the difference between the insulation powers of the alternative exchange regimes.

Similarly, in Marion's (1981: 63) model, wealth effects of exchange rate changes "play a crucial role in the transmission of foreign disturbance to the small economy". This is because changes in exchange rate affects the level of wealth, which also affects demands for all goods and assets. Therefore, the general result from studies that incorporate the wealth effects of exchange rate changes is that the difference between the alternative exchange rate regimes, with respect to insulation power, is somewhat small.

Overall, the conventional wisdom has identified the degree of openness, position in foreign-currency denominated assets, factor mobility, wage and price indexation process, sources of economic disturbances and institutional set up as the most important factors in the determination of the optimal exchange market. The consideration of these factors has led many experts in the 1970s to have suggested fixed rates for the LDCs. This conventional wisdom led Lewis ((1979: 18) to say:

> "It is now the conventional wisdom that the currencies of the developed countries should float, but the currencies of the less developed countries (LDCs) should not; that is to say that each LDC should choose a more developed country (MDC) as a partner, or the Special Drawing Rights (SDR) and tie itself in a fixed relationship."

II.1.5 Administrative Corruption

However, since mid-1980s, the view of the World Bank (International Bank for Reconstruction and Development, IBRD) and the International Monetary Fund (IMF), especially those emanating from case studies on Performances of Structural Adjustment Programmes in the LDCs, are unambiguous in recommending floating rates for all countries (i.e. including all LDCs). This shift was informed by the high incidences of administrative corruption when fixed rates were in place, especially in countries like Nigeria where foreign exchange from the primary exports (e.g. oil) accrue in the main to the government, the operation of fixed rate had always resulted in an over-valued currency sustained by import and exchange controls. Such reliance on administrative controls in allocating the scarce foreign exchange had often created room for influence peddling and rent-seeking behaviour that saw the rent associated with foreign exchange scarcity escaping from government coffers and appropriated to those who are close to the corridors of power. Thus, the adoption of floating rates by such governments would at the minimum improve their budget.

II.2 The Conventional Wisdom on Optimal Exchange Rate Regime

Considering the factors mentioned above and based on some empirical findings, economists over time have had some consensus on the optimal foreign exchange rate regime for every category of economies. However, the conventional wisdom in this regard has been changing with time. For instance, between 1900 and 1929, the conventional wisdom was that all economies should operate fixed rates. However, between 1930 and late 1960s, the conventional wisdom was that less developed countries (LDCs) should float, while more developed countries should maintain fixed rates. Between early 1970s and early 1980s, the conventional wisdom was that the LDCs should not float, while the developed countries should. Today, the dominant view is that all countries – whether developed or less developed - should float. These changes in the state of the conventional were aptly described by Lewis (1979:20):

> "From 1900 to 1929 the consensus of economists was that all countries, whether more or less developed should maintain fixed exchange rates. However, from 1930 to 1965, it was increasingly felt that primary producing countries (even rich Australia) has special problems. Our current consensus that the developed should peg, is the exact opposite or what had nearly become the consensus only twelve years ago."

The changing state of the conventional wisdom is the result of the ever increasing number of studies that have continuously modified our thinking. Since the early 1980 till date, the conventional wisdom has been that all countries should float.

III. Optimal Exchange Rate Regime and the Nigerian Experience

An examination of the factors mentioned in Section 2 above with respect to Nigeria and our earlier analysis suggested that the value of foreign currency denominated assets, and institutional set-up were not the major factors in deciding the optimal exchange rate regime for Nigeria. Rather, the most relevant factors were the source of disturbances to her external balance, extent of corruption/positive budgetary effects on government and degree of openness and diversification. Because the shocks to the economy, especially her external balance indicators come dominantly from foreign economies and because corruption is highly tolerated in the economy as well as the positive budgetary effects of floating rates on government budget, the benefits of floating rates appear to outweigh the benefits that fixed rates would bring as result of her high openness, undiversified production and diversified consumption.

Besides these considerations, a peculiar characteristic of the Nigerian external sector tends to blur the distinction between a flexible and fixed exchange rate regime. In the Nigerian situation, the government is the major foreign exchange earner through its receipts from oil rents. Consequently, the government would be the principal supplier of foreign currencies into the foreign exchange market. This being the case, the government would be able to determine independently what proportion of her foreign exchange receipts she would not monetise since she is not compelled to provide domestic currency equivalent for its foreign exchange holding because it does not accrue to the private sector in the first instance. Given this, the government could make the FLER work more or less like the FXER, by using long-run factors rather than the erratic, short-run market forces to determine her supply of foreign currencies to the flexible exchange market. This way, the FXER may outperform the FLER.

Hence, if Nigeria could do away with corruption, Marston's (1982) testimony best describes the Nigerian policy options:

> "As far as the choice between fixed and flexible rate is concerned, flexible rates generally exhibit less output variation than fixed rates, but it is possible for the opposite to be true."

III.1 The Nigerian Experience

Between 1959 and 1967, Nigeria operated a fixed exchange rate regime in which the Nigerian pound was fixed at par with the British pound. In 1967 when the British pound was devalued, the Nigerian monetary authorities switched the peg to US dollar i.e. the Nigerian pound was pegged to the US dollar; during this period, severe exchange restrictions were put in place (Nnanna, 2001).

In 1970, following the financial crisis suffered by the world payments system and the devaluation of the dollar, the Nigerian pound was pegged again to the British pound. On January 1, 1973, Nigeria introduced the naira to replace the Nigerian pound at the rate of N2 to one Nigerian pound and pegged this currency to the US dollar. In 1978, Nigeria pegged the naira to a basket of 12 currencies of its major trading partners. The practice of pegging to a basket of currencies continued until September 1986 when a variant of flexible exchange rate system was introduced. Thus, between 1959 and 1986, Nigeria operated a fixed exchange rate regime. However, this fixed rate regime all along had coexisted with a flourishing parallel foreign exchange market that had existed since World War II (Pick, 1984). The parallel foreign exchange market became more noticeable since 1962 when the Exchange Control Act, 1962 was enacted.

Since September 1986 till date, Nigeria has operated a variant of a flexible exchange rate regime, except in 1994 when the floating rate was suspended and the naira was fixed at the prevailing market determined rate of N22 to a dollar. But this flexible rate continued to co-exist with a parallel foreign exchange market that is either *de facto* or *de jure* legalised.

Similarly, in 1989, Bureau-de-change was introduced (CBN, 2003: 17-22). On March 5, 1992, the monetary authorities unified the official exchange rate with the parallel rate, moving the official rate from its prevailing rate of N10.56 to a US dollar to N18.0 to a US dollar (which was the then prevailing parallel rate). The records of Nigeria's exchange rate policies and the prevailing conventional wisdom on the subject are summarised in Table1. Therefore, Nigeria operated a fixed rate between 1959 and 1986 and a flexible rate since September 1986. Thus, for most part of its foreign exchange history, it had been guided by the prescription of the prevailing Conventional Wisdom at the time (see Table 1). The only exceptions were between 1965 and 1969 and between January 1980 and August 1986.

Table 1: Conventional Wisdom on Optimal Exchange rate Regime and Nigeria Exchange Policies by Time

Period	Conventional Wisdom	Nigerian Exchange rate Regime
1900 - 1929	Fixed rate recommended for all countries	Fixed
1930 - 1964	Fixed rate recommended for all developed countries, but LDCs seen as having special needs (for floating)	1930- 58: Fixed; 1959-64: Fixed - Nigerian pound fixed to British pound
1965 - 1969	Fixed rate recommended for all developed countries; floating rates recommended for all LDCs.	1965- 66: Fixed - Nigerian pound fixed to British pound; 1967-69: Fixed - Nigerian pound fixed to US$
1970 - 1980	Floating rates recommended for all developed countries; fixed rate recommended for all LDCs.	1970-72: Fixed - Nigerian pound fixed to British pound; 1973-77: Fixed - Nigerian naira fixed to US$; 1978-80: Fixed - Nigerian naira fixed to a basket of 12 currencies
1981 - To Date	Floating rates recommended for all countries.	1980- 1986 (Aug.): Fixed - Nigerian naira fixed to a basket of currencies; 1986 (Sep.) - 2015: Floating; except 1994

Sources: Relevant Literature; CBN (Various Issues) and Nnanna (2001)

In the case of 1965-1969, the Nigerian monetary authorities weathered the storm from its disobedience by changing the currency from the currency it was pegged to, thereby achieving some limited degree of exchange rate flexibility. However, between January 1980 and August 1986 when the conventional wisdom recommended floating rates for all countries and Nigeria was operating troubled fixed rate, the adverse consequences were more severe.

There were significant and persistent balance of payments deficits and the associated loss of foreign reserves (from US$5.6billion in 1980 to US$0.2billion in 1983), inflation was ravaging (from single digit in 1980 to 23 per cent in 1983 and 40 per cent in 1984), stagnation and decline in level of economic activities (at a minus 8 per cent in 1981 and negative 7 per cent in 1984) and high-level unemployment was the order of the day (at 6 per cent in 1984) (see Table 2).

The Nigerian authorities remained defiant. Rather than abide by the conventional wisdom, it put in place a set of expenditure-changing (expenditure-reducing) policies, documented in its Economic Stabilisation Act, 1982, when expenditure-switching policies, like floating rates or parity changes, were needed. As the expenditure reducing policies reduce the national output with multiplier effects, outputs were reduced in greater proportions than the reduction in government expenditure that brought them about. The

result was that fiscal indicators worsened as fiscal deficit as percentage of national output worsened from negative 8.0 per cent in1981 to 12.0 per cent in 1982 (Table 2).

Table 2: Values of Some Key Macroeconomic Variables in Nigeria (1979-1989)

YEAR	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
Real GDP	212,665.40	224,018.70	205,222.10	199685.3	185,598.10	183,563.00	201,036.30	205,971.40	204,806.50	219,875.60	236,729.60
Real GDP Growth Rate (%)	2.5	5.3	-8.4	0.5	-4.1	-6.7	7.9	3.2	1.8	4	7.3
Fiscal Deficit/GDP (%)			-8.19	-12.44	-6.34	-4.46	-4.48	-11.94	-5.6	-8.74	-6.98
Price of Crude Oil ($/Barrel)	29.31	43.69	41.74	37.16	33.95	33.57	31.43	16.86	20.72	17.36	21.4
Official Exchange rate (N/$) avg	0.596	0.546	0.61	0.673	0.724	0.765	0.894	2.021	4.018	4.537	7.392
Inflation Rate (%)	11.59	9.87	21.04	7.62	23.23	39.62	5.49	5.4	10.15	56.07	50.5
Unemployment Rate (%)		6.4				6.2	6.1	5.3	7	5.3	4.5
Parallel Rate (N/$)	0.9804	0.9346	0.9346	1.2195	4.1667	3.5714	3.7037	7.6923	6.25	8.35	9.46
Foreign Reserves ($'M)	3,109	5,622	2,441.60	1,043.30	224.4	710.1	1,657.90	2,836.60	7,504.60	5,229.10	3,047.60
Exchange Rate Premium (N/$)	0.38	0.39	0.32	0.55	3.44	2.81	2.81	5.67	2.23	3.81	2.07
Exchange Rate Premium (%)	65	71	53	81	475	367	314	281	56	84	28

The crisis did not abate until 1986 when a floating rate was introduced, which brought Nigeria into alignment with the conventional wisdom. Table 3 provides some summary picture on the comparative macroeconomic performance of Nigeria for 1961-2011 and it showed that the period 1981-1985 was particularly bad on virtually all indicators, compared with other periods.

Table 3: Values of Some Key Macroeconomic Variables in Nigeria 191-2011 (5-Year Average)

Period	1961-65	1966-70	1971-75	1976-80	1981-85	1986-1990	1991-95	1996-2000	2001-2005	2006-2010	2011
Real GDP	84,740.86	96,722.50	176,100.69	214,986.10	195,020.93	226,986.64	273,687.07	309,604.03	471,447.64	679,355.67	833,379.92
Real GDP Growth Rate (%)	5.2	9.3	7.1	3.9	-2.2	4.9	2.7	3.1	7.1	6.7	7.5
Fiscal Deficit/GDP(%)					-7.2	-8.3	-7.2	-3.0	-2.8	-1.7	
Price of Crude Oil ($/Barrel)	3.4	3.8	7.8	24.5	35.6	20.7	20.7	22.2	37.6	77.4	113.8
Official Exchange rate (N/$)(avg)	0.7	0.7	0.7	0.6	0.7	5.2	30.5	87.8	125.4	134.3	153.9
Inlation Rate (%)	2.8	6.4	14.4	15.5	19.4	25.9	48.9	12.3	15.7	10.3	10.9
Unemployment Rate (%)						5.1	2.6	3.3	3.2	17.2	23.9
Parallel Rate (N/$)	0.7	0.9	0.9	1.1	2.7	8.4	52.4	94.8			
Foreign Reserves($'M)	182.0	115.2	1,592.2	3,219.6	1,215.5	4,631.9	3,550.7	6,613.7	14,159.7	44,270.7	32,630.3
Exchange Rate Premium(N/$)	0.0	0.2	0.3	0.4	2.0	3.2	21.9	7.0			
Exchange Rate Premium(%)	3.7	30.8	41.1	74.1	258.2	94.8	103.1	7.7			

Some caution must be exercised when comparing macroeconomic performance of 1981-1985 fixed exchange rate regime with that of 1986-1990 floating rate. The price of crude fell significantly from a five-year average of US$35.6 per barrel in 1981-1985 to US$20.7 in 1986-1990. Similarly, five-year average price of crude oil was US$20.7 per barrel in the floating period of 1991-1995. Consequently, it was a long-period of bad luck for Nigeria in the oil market. This tended to conceal the otherwise good performance of the floating exchange rate policy of that period.

Furthermore, there were a few false steps in the management of the floating rate and some adjustment/learning costs. For instance, the effort to unify the official exchange rate with the parallel rate was not well founded. There will always be a wedge (negative or positive) between the official and parallel rates because of the differences in the needs of

the two markets. Parallel markets for foreign exchange cater for the convenience and confidentiality needs of users of those markets. They also provide cover for proceeds of illegal transactions (e.g. proceeds from administrative corruption, illicit trade, including drug business and smuggling) (Jimoh,1992). On account of these and more, there will always be a difference between the official and the parallel exchange rates. It was, therefore, an error to have wanted to unify the two rates without an adjustment for differences in their basic features. All these had dwarfed the excellent performance of the floating rates.

IV. Concluding Remarks

This paper examined the Nigerian exchange rate experience in the context of the conventional wisdom on the subject. It noted that since the 1960s, Nigerian exchange rate policies had largely obeyed the prescriptions of the conventional except between 1981 and 1985. It noted that during this period, macroeconomic variables worsened significantly and reached a crisis state. The crisis was resolved only with the adoption of floating rates in 1986 and the good performance of the floating rates were often concealed by major negative external shocks that were recorded during this period as well as some few initial false steps that were taken by monetary and fiscal authorities. In particular, the paper noted that exchange rate unification policy of March 1992 may have been inadequately conceived.

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