ISSN No: -2456-2165 https://doi.org/10.38124/ijisrt/26apr1277

Domestic Refining and Energy Diversification in Post-Subsidy Nigeria

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Publication Date: 2026/05/06

Abstract: This study aims to examine the impact of fuel subsidy removal on Nigeria's economic trajectory. We hypothesized that the removal of petroleum subsidies does not generate inflationary pressures and test this hypothesis using the Dynamic Simulated Autoregressive Distributed Lag (DS-ARDL) framework. The outcome of the study shows that fuel-subsidy removal has a significant impact on the cost of living and inflation level in Nigeria, indicating that as 1 unit of subsidy removal increases, the cost of living and inflation level increase by 73.8%To address these challenges, the government began promoting alternative energy sources such as Compressed Natural Gas (CNG), solar energy, and Liquefied Petroleum Gas (LPG). These alternatives are cheaper and more sustainable in the long run. This paper therefore examinesd how domestic refining and energy diversification can help Nigeria achieve economic stability and energy security in the post-subsidy era. Based on existing data, prior to 2023, domestic refining remained extremely low. However, the emergence of new private refining capacity, with the establishment and operation of the Dangote Refinery and refinery rehabilitation programs has begun to increase domestic refining activities. Strengthening domestic refining capacity through continued investment; expanding renewable energy development, particularly solar power; improving regulatory stability to attract private sector participation; developing gas-based industrialization to support energy diversification and investing in energy infrastructure including pipelines and storage facilities were recommended.

Keywords: *Domestic Refining, Dynamic Stimulated Autoregressive Distributed Lag (DS-ARDL), Energy Diversification, Fuel Subsidy.*

JEL Code: *B5, H2, G5.*

How to Cite: Adebanwa, Ayowole Abayomi; Olaosebikan, Oluwadamilola Ilerioluwa; Taiwo Adeola Oluwabunmi; Alabi, Opeyemi Enitan (2026) Domestic Refining and Energy Diversification in Post-Subsidy Nigeria. *International Journal of Innovative Science and Research Technology*, 11(4), 3364-3372. https://doi.org/10.38124/ijisrt/26apr1277

I. INTRODUCTION

Nigeria is one of Africa's largest producers of crude oil, yet the country has historically relied on imported refined petroleum products due to limited operational refining capacity. Despite possessing four state-owned refineries with a combined installed capacity of approximately 445,000 barrels per day, persistent operational inefficiencies and maintenance challenges have led to extremely low utilization rates (NNPC, 2023). Consequently, the country relied heavily on imports to meet domestic fuel demand, thereby increasing pressure on foreign exchange reserves and worsening fiscal imbalance.

The removal of fuel subsidies by the Nigerian government in 2023 marked a major shift in the country's energy policy framework. Historically, fuel subsidies served as a critical mechanism for stabilizing domestic fuel prices and mitigating the cost of living for households. However, the policy imposed substantial fiscal strain on government finances, with subsidy expenditures running into several trillions of naira annually and projected to account for as much as 3% of GDP if continued (NNPC, 2023). The reform

ISSN No: -2456-2165 https://doi.org/10.38124/ijisrt/26apr1277

aimed to reduce fiscal burdens, encourage private investment in refining infrastructure, and promote a more efficient downstream petroleum market (World Bank, 2024). This growing fiscal burden provided a strong rationale for the policy's removal.

In spite of these expected gains, the immediate effects of the subsidy removal have been accompanied by notable economic challenges and welfare concerns. Empirical data showed that the pump price of petrol increased sharply from approximately ₦238 per litre in May 2023 to over ₦545 shortly after the announcement, and further escalated to about ₦1,184 by October 2024, reflecting an increase of nearly 88% within a one-year period. This substantial rise in fuel prices has generated widespread ripple effects across the economy, particularly through elevated transportation and production costs (Ozili and Obiora, 2023).

Consequently, inflationary pressures have intensified significantly. According to data from the National Bureau of Statistics, Nigeria's headline inflation rose from 28.9% in December 2023 to 34.19% by June 2024, representing the highest level recorded in nearly two decades. Empirical evidence further demonstrated that subsidy removal has a statistically significant impact on living costs, with simulation results indicating that a marginal increase in subsidy withdrawal could raise inflation and cost of living by as much as 73.8% (Ajuwon & Abiodun,2025). This has contributed to a pronounced decline in real incomes and a worsening cost-of-living crisis.

The sectoral implications have also been severe. For instance, the transport sub-sector is highly sensitive to fuel price changes in Nigeria. It experienced a 50.64% contraction in GDP in the second quarter of 2023, largely attributed to the effects of subsidy removal (NBS, 2023). At the household level, rising fuel costs have translated into higher food prices and general consumption expenditure, exacerbating food insecurity. Recent evidence suggests that over 31 million Nigerians are facing acute food shortages, driven in part by rising costs associated with subsidy removal and inflationary pressures.

Empirical evidence indicated that the Nigerian naira has undergone sustained depreciation over the past decade, underscoring the fragility of the country's foreign exchange base. According to the Central Bank of Nigeria, the official exchange rate moved from approximately ₦197/$1 in 2015 to about ₦461/$1 in 2023, while the parallel market rate exceeded ₦700/$1 within the same period (CBN, 2023). This trend reflects Nigeria's heavy dependence on crude oil exports, which accounted for over 80% of foreign exchange earnings as reported by the National Bureau of Statistics (NBS, 2023). The implication is heightened exposure to global oil price volatility, resulting in exchange rate pressures, imported inflation, and rising production costs for domestic industries.

Energy diversification has been widely recognized as a strategy for enhancing energy security and reducing vulnerability to supply shocks (International Energy Agency, IEA, 2022) advocated that diversified energy systems are more resilient and better able to maintain supply stability during global market disruptions. Thus, scholars have argued that the country's overreliance on crude oil exports and imported refined products represents a structural inefficiency in the energy economy (Adenikinju, 2019). Hence, domestic refining could significantly reduce foreign exchange pressures and improve downstream sector efficiency.

The entry of large-scale private refining projects, particularly the Dangote Refinery, represents a major structural shift in Nigeria's downstream petroleum sector. With a nameplate capacity of 650,000 barrels per day, the refinery has the potential to significantly reduce Nigeria's dependence on imported petroleum products (IEA, 2023).

Therefore, the removal of fuel subsidies has significantly exacerbated inflationary pressures in Nigeria (NBS, 2024). For example, inflation in Nigeria rose from 28.9% in December 2023 to 29.9% in January 2024. It continued its upward trajectory, reaching 34.19% by June 2024, marking the seventh consecutive monthly increase and the highest level recorded in nearly two decades. This inflationary trend has been largely driven by rising fuel and food prices, coupled with currency depreciation, and has deepened the cost-of-living crisis (NBS, 2025).

Therefore, this study examined the need for energy diversification and domestic refining in post-subsidy Nigeria. Other sections of this paper is divided into four sections. Section II discussed the conceptual, theoretical and empirical review of existing literature while section III covered the research methodology including data and data sources and the estimation technique adopted for the study. Section IV discusses the findings revealed in the research while section V concluded the paper with valuable recommendations based on the economic implications of the research work.

II. LITERATURE REVIEW

This section examined existing studies and theories related to subsidy removal, domestic refining, and energy diversification. It also provided background understanding of how these concepts affect Nigeria's economy.

➢ *Conceptual Review*

- *Concept of Fuel Subsidy Removal*

Fuel subsidy removal entails the withdrawal of government intervention that previously reduced the retail price of petroleum products below market cost. In Nigeria, this policy shift represents a transition from regulated pricing to a market-determined pricing mechanism. Yunusa, Yakubu, Emeje, Ibrahim, Stephen & Egbunu (2023) asserted that the removal of subsidy in 2023 led to a sharp increase in petrol prices, with average pump prices rising from about ₦219 per litre before removal to approximately ₦655 per litre within one year (a 199% increase). This caused untold hardship on Nigerians in terms of the cost of living.

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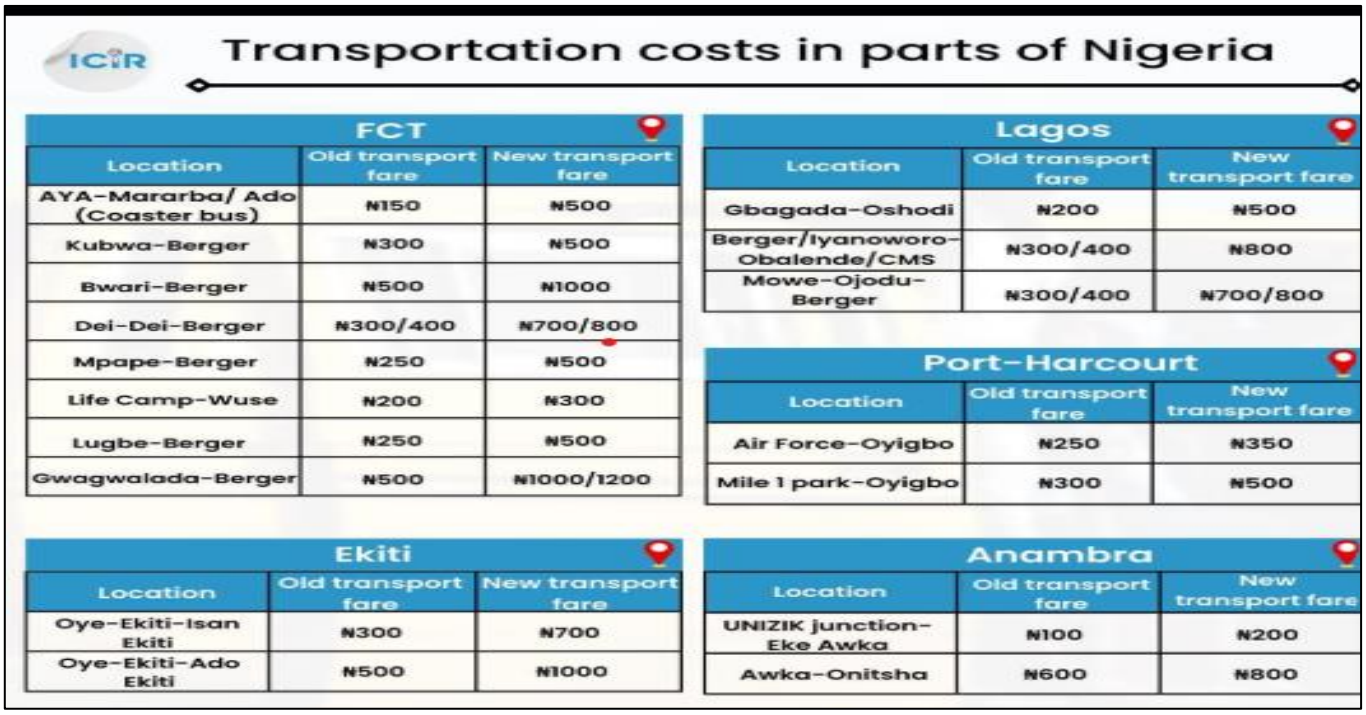
Fig 1 Excerpt of Long Queues at Different Fuel Filling Stations Across States in Nigeria

The scarcity has led to passengers waiting longer at bus stops and paying higher fares. Furthermore, this price adjustment significantly transmitted into the broader economy. For instance, empirical evidence showed a strong correlation (r = 0.93) between petrol price changes and inflation, with fuel price variations explaining 87.1% of inflationary movements in Nigeria. CBN (2025) indicated that 90.8% of firms identify energy costs (fuel and electricity) as the primary driver of inflation (Adebanwa, et al, 2026) . While subsidy removal improves fiscal sustainability by reducing government expenditure, it simultaneously induces cost-push inflation and welfare losses, particularly among low-income households, particularly in the area of transporation costs. A cursory look at Fig. 2 below, exemplifies this assertion:



Transportation costs in parts of Nigeria

FCT

Location	Old transport fare	New transport fare
AYA-Mararba/ Ado (Coaster bus)	₦150	₦500
Kubwa-Berger	₦300	₦500
Bwari-Berger	₦500	₦1000
Dei-Dei-Berger	₦300/400	₦700/800
Mpape-Berger	₦250	₦500
Life Camp-Wuse	₦200	₦300
Lugbe-Berger	₦250	₦500
Gwagwalada-Berger	₦500	₦1000/1200

Lagos

Location	Old transport fare	New transport fare
Gbagada-Oshodi	₦200	₦500
Berger/Iyanoworo-Obalende/CMS	₦300/400	₦800
Mowe-Ojodu-Berger	₦300/400	₦700/800

Port-Harcourt

Location	Old transport fare	New transport fare
Air Force-Oyigbo	₦250	₦350
Mile 1 park-Oyigbo	₦300	₦500

Ekiti

Location	Old transport fare	New transport fare
Oye-Ekiti-Isan Ekiti	₦300	₦700
Oye-Ekiti-Ado Ekiti	₦500	₦1000

Anambra

Location	Old transport fare	New transport fare
UNIZIK junction-Eke Awka	₦100	₦200
Awka-Onitsha	₦600	₦800

Fig 2 Transportation Costs in Parts of Nigeria as a Result of Fuel Scarcity in 2023.

➢ *Energy Diversification*

Energy diversification refers to the strategic expansion of a country's energy sources beyond dominant reliance on fossil fuels, particularly crude oil. Conceptually, it aligns with energy security and sustainable development paradigms, which emphasize reducing exposure to external shocks. Nigeria's heavy dependence on oil makes it vulnerable to global oil price volatility and exchange rate fluctuations, which directly affect domestic fuel prices and macroeconomic stability.

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Empirical insights reinforce this necessity: energy costs remain a dominant structural constraint in Nigeria, with businesses consistently citing fuel and electricity as the most significant contributors to production costs and inflationary pressure. Thus, diversification into renewable sources (solar, hydro, wind) is critical for.

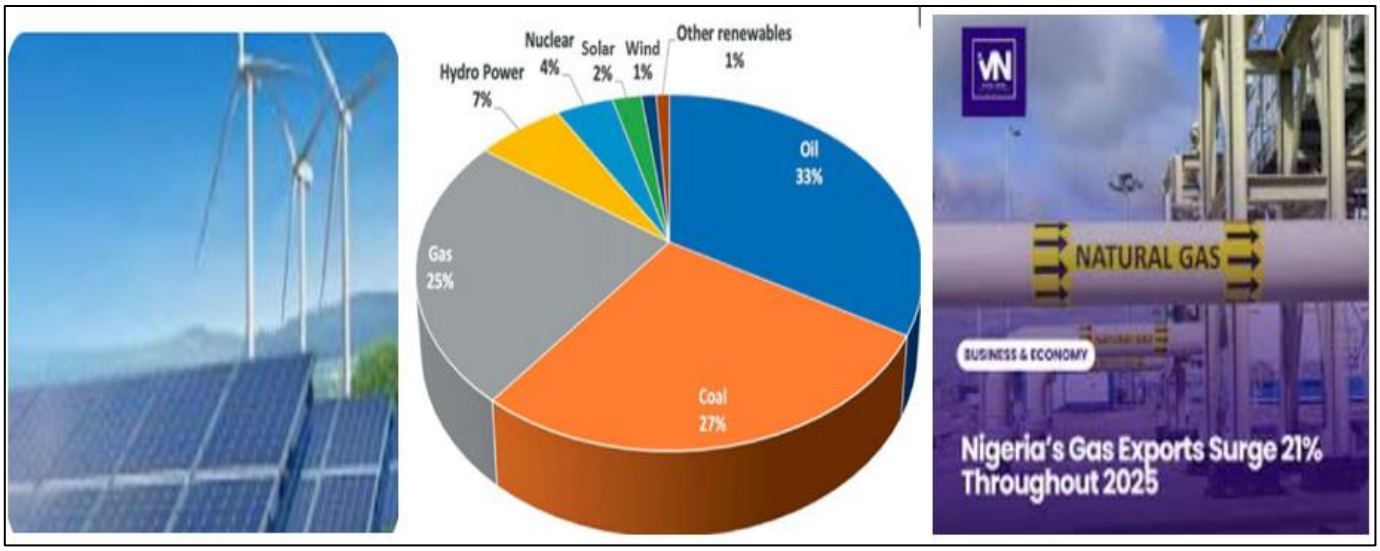

Fig 3 Energy Diversification in Nigeria: Prospects and Problems

- *Domestic Refining*

Domestic refining can be viewed as the conversion of crude oil into finished petroleum products within a country's domestic economy, rather than exporting crude and importing refined outputs. This move is central to economic transformation, as it promotes industrialization, enhances domestic production capacity, and increases the contribution of the oil sector to overall economic output (Adebanwa, Emmanuel, Akerele & Ajayi, 2026). The Dangote Refinery has the capacity to produce over 30 million litres of petrol daily. Thus, domestic refining accounted for more than half of national petrol supply by early 2026 before the outbreak of war between Israel and Iran.

Fig 4 Excerpts of Domestic Refining in Nigeria

➢ *Theoretical Review*

Some relevant theories that discussed energy diversification and domestic refining in post-subsidy Nigeria includes the following out of which our study is based on the Structural Change Theory:

- *Structural Change Theory*

Lewis (1954); Chenery (1983) advocated that economic development involves shifting from a mono-sector (e.g., oil) to a diversified multi-sector economy (industry, energy mix, services). Hence, this theory explains the basis for energy diversification as to achieve structural transformation of the Nigerian economy. Hence, it is expected that the removal of fuel subsidy in 2023 should force market pricing, incentivize efficient sectoral reallocation towards productive domestic energy industries, but these are yet to be economically realized in the post-subsidy era. Hence, this paper explored the journey so far by identifying the areas of prospects for the success of the project – Nigeria.

- *Resource Curse Theory (Paradox of Plenty)*

Jeffrey D. Sachs and Andrew M. Warner (1995); Max Corden and J. Peter Neary (1982) explained why countries endowed with abundant natural resources often experience slower economic growth, weak institutions, and poor development outcomes. Auty (1993) first systematically

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coined the term *resource curse* but later other Proponents such as Sachs and Warner (1995, 2001) empirically demonstrated that resource-rich countries tend to grow more slowly. They asserted that resource abundance leads to overdependence on a single commodity, crowding out diversification. Also, Terry (1997) linked oil wealth to weak institutional development while Ross (2013) showed how oil wealth undermines democracy and economic diversification. The *Dutch disease* effect, oil price and revenue volatility, rent seeking and state capture were some of the core mechanisms through which Resource curse theory was explained.

Hence, this theory is also relevant to this study as Nigeria exemplifies the resource curse in the sense that oil accounts for the majority of her export earnings and a large share of government revenue while the non-oil sectors remain underdeveloped despite vast potentials.

- *Dependency Theory*

The Nigerian experience provided a compelling case study for Dependency Theory. Despite being rich in natural resources particularly crude oil Nigeria remains heavily dependent on the export of raw materials and the importation of refined products and consumer goods. This economic structure exposes the country to volatile global markets and terms-of-trade shocks, limiting its capacity to achieve long-term, self-sustained growth. Consequently, over 80% of Nigeria's export earnings come from oil, yet the country imported refined petroleum products thus being import-dependent. Hence, Nigeria continued to struggle with widespread poverty and under-development. This theory advocated for a re-thinking of global economic relationships and called for more autonomous development strategies such as industrialization, economic and energy diversification, and regional trade integration that can reduce dependence on imports and empower domestic growth.

➢ *Empirical and Methodological Review*

Adewuyi and Adeleke (2017) examined the nexus between economic diversification and energy efficiency in Nigeria using a two-stage efficiency model. Their findings revealed that diversification improves both energy and carbon efficiency over time, particularly in the post-1998 period, although environmental inefficiencies persisted in earlier decades. However, the domestic refining effect of Dangote Refinery was not in view as that then.

Similarly, Gil-Alana and Umeh (2021) indicated a strong linkage between energy consumption and economic growth. Using OLS regressions with fractionally integrated errors, they revealed that electricity consumption, oil prices, electricity prices, real interest rate and employment significantly affect GDP per capita with only real interest rate having a negative relationship with GDP per capita.

In another sense, Obele (2025) and Wakili, Abubakar, Adamu & Jajere (2025) employed ARDL to estimate both short-run and long-run relationships between refinery output, fuel prices, exchange rates, and import dependence. While Obele (2025) examined the effects of government policy frameworks on the diversification from crude oil to alternative energy in Nigeria**,** he opined that Energy Transition Plan (ETP), Petroleum Industry Act (PIA) 2021, Electricity Act 2023, and the National Renewable Energy and Energy Efficiency Policy (NREEEP) alongside NERC Mini-Grid Regulations significantly influenced investment in alternative energy, promotion of natural gas, renewable energy generation, and rural electrification. Conversely, he noted that the challenges hindering policy frameworks did not significantly constrain diversification efforts.

Wakili, Abubakar, Adamu & Jajere (2025) explored the potentials and challenges of Economic Diversification through Solid Minerals Sector in Nigeria. They adopted Documentary Research Method to present their findings. They revealed that solid mineral had a positive but statistically insignificant impact on economic growth in Nigeria while Ajao and Sadeeq (2023) highlighted the economic viability of diversifying Nigeria's energy mix through electric vehicle infrastructure and renewable energy integration, emphasizing the need for policy frameworks that support transition away from oil dependency. However, none of these research works examined the impact of domestic refining efforts of Dangote Refinery in Nigeria.

III. RESEARCH METHODOLOGY

This study adopted a critical discourse analysis using secondary data sources. Data were collected from government publications, international energy reports, and academic literature. to examine trends in domestic refining capacity, energy diversification efforts, and policy changes following subsidy removal.

The secondary data were sourced from OPEC Statistical Bulletin; NNPC Annual Reports

➢ *Presentation of Findings*

Table 1 Nigeria Crude Oil Production Trend (Million Barrels per Day)

Year	Crude Production (mb/d)
2018	1.93
2019	2.0
2020	1.79
2021	1.63
2022	1.4
2023	1.38
2024	1.5

Source: OPEC Statistical Bulletin; NNPC Annual Reports.

ISSN No: -2456-2165 https://doi.org/10.38124/ijisrt/26apr1277

Table 2 Estimated Domestic Refining Output (mbpd)

Year	Refining output (mbpd)
2018	60
2019	55
2020	30
2021	20
2022	15
2023	25
2024	120

Source: NNPC, 2024

Table 3 Summary of Macroeconomic Indicators (2023 vs 2026)

Indicator	Pre-Subsidy (Q1 2023)	Post-Subsidy (Q1 2026)
Fuel Subsidy Cost	₦400bn per month	₦0 (Official)
FAAC Monthly Share	~₦650bn	~₦1.2tn - ₦1.4tn
Headline Inflation	22.04%	~15.06% (Moderating)
Exchange Rate (Official)	₦461/$	₦1,480/$

Table 4 Nigeria's Refining Capacity and Operational Status (March 2026)

Refinery Name	Status	Installed Capacity (bpd)	Current Output / Notes
Dangote Refinery	Active	650,000	Operating at ~85% capacity; plans to hit 700,000 bpd by late 2026.
Old Port Harcourt Refinery	Suspended	60,000	90% rehabilitated but shut down in May 2025 due to "sub-commercial" operational costs.
New Port Harcourt Refinery	Dormant	150,000	Part of the larger PHRC complex; currently undergoing phased rehabilitation.
Warri Refinery	Suspended	125,000	Briefly restarted in early 2025 at 60% capacity but was shut down again by April 2025.
Kaduna Refinery	Dormant	110,000	Undergoing rehabilitation; NNPC Limited target for technical partners is June 2026.
Aradel (Ogbabele)	Active	11,000	Operational modular refinery providing diesel and kerosene.
OPAC Refinery	Active	10,000	Operational modular plant in Kwale, Delta State.
Waltersmith Refinery	Active	5,000	Phase 1 operational; Phase 2 (expansion to 30,000 bpd) in progress.
Edo Refinery	Active	1,000	Small-scale modular plant focused on niche products.
Duport Midstream	Active	2,500	Energy park model refinery in Edo State.

➢ *Summary of National Refining Performance*

- Total Installed Capacity: Approximately 1.125 million bpd (Conventional + Modular).
- Active Functional Capacity: Roughly 680,000 bpd, with the Dangote Refinery alone contributing nearly 96% of the current domestic fuel supply.
- Refinery Utilization: Recent reports from the NMDPRA indicate a 61.5% utilization rate due to technical hitches and crude supply limitations

Table 5 Energy Source Cost-Benefit Analysis (March 2026)

Energy Type	Primary Application	Monthly Cost Index	Adoption Barrier
PMS (Petrol)	Private Cars/Gen	Very High	High Pump Price
CNG (Gas)	Commercial Buses	Low	High Conversion Cost
Solar PV	SMEs/Homes	Zero (Variable)	High Initial Capex
LPG (Gas)	Cooking	Moderate	Safety/Access Gaps

Table 6 Comparative Impact Matrix (2023–2026)

Sector	Nature of Impact	Mitigation Strategy	Efficacy Level
Transport	200% Fare Hike	CNG Bus Deployment	High (Urban)
SMEs	300% OPEX Hike	Solar Grants/Loans	Medium
Households	40% Food Inflation	Cash Transfers/Wage Award	Low-Medium
Civil Service	Income Erosion	₦70k Minimum Wage	Medium

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Table 7 Strategic Outlook (2026–2027)

Challenge	Impact	Strategic Mitigation
Crude Theft	Lowers DCSO	Enhanced digital pipeline surveillance
Logistics	High "Bridging" Costs	Rehabilitation of Rail & System 2B
Pricing	Inflationary Pressure	Scaling CNG to 1m vehicles by 2027
Forex	Naira Volatility	Full transition to Naira-for-Crude

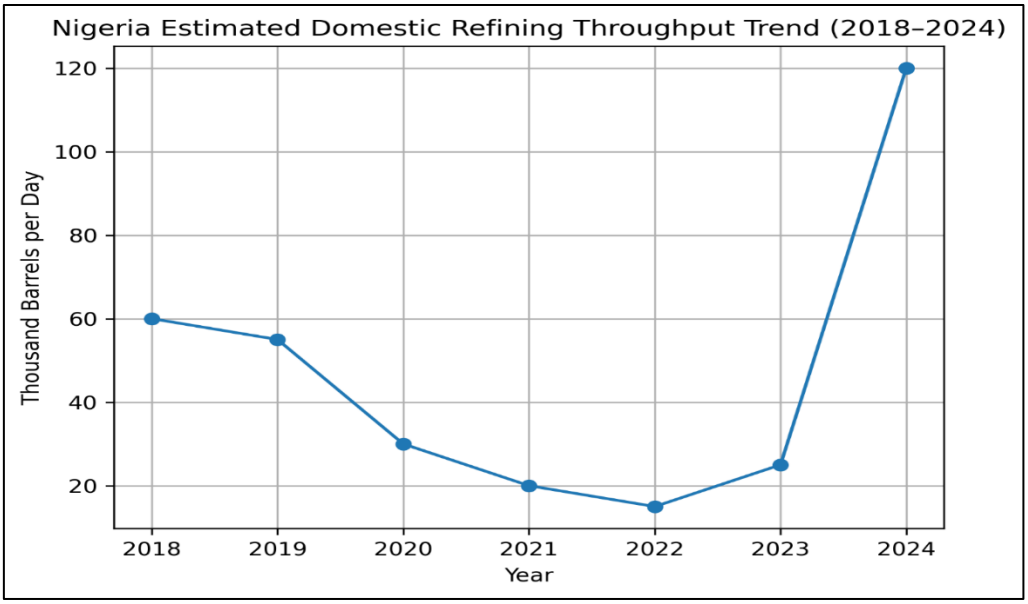

Fig 5 Trend in Domestic Refining Throughput

The data indicated that domestic refining throughout from 2018 to 2024 remained low probably due to the outbreak of COVID 19 and the consequent refinery shutdowns and business operational challenges. However, the emergence of new private refining capacity, with the establishment and operation of the Dangote Refinery and refinery rehabilitation programs has begun to increase domestic refining activities. Hence, increased refining capacity is expected to significantly reduce Nigeria's reliance on imported petroleum products.

Additionally, Nigeria possesses substantial renewable energy potentials. Solar irradiation levels in northern Nigeria are among the highest globally, providing strong potential for large-scale solar energy deployment (IRENA, 2022). The expansion of renewable energy could play a significant role in reducing reliance on fossil fuels and improving energy access.

IV. CONCLUSION AND RECOMMENDATIONS

The findings indicated that Nigeria's persistent reliance on crude oil exports, alongside its dependence on imported refined petroleum products, has limited economic stability, intensified fiscal pressures, and increased susceptibility to external shocks in global energy markets.

The analysis further demonstrates that expanding domestic refining capacity is crucial for correcting the imbalance between resource availability and energy sufficiency. Nevertheless, refining capacity alone is insufficient to ensure long-term stability. A broader energy mix that incorporates renewable energy sources—alongside natural gas—remains vital for reducing structural dependence on fossil fuels, enhancing environmental outcomes, and ensuring a reliable energy supply.

In addition, the study identifies weak institutional frameworks and inconsistent regulatory practices as major impediments to investment and sectoral growth. The absence of a stable policy environment has discouraged private sector participation and slowed reform efforts. Compounding this challenge is the inadequacy of critical energy infrastructure, including pipelines, storage systems, and transmission facilities, which continues to constrain efficient energy distribution.

In essence, the study concludes that Nigeria's pursuit of energy security and economic diversification depends on a well-coordinated strategy that integrates domestic refining expansion, renewable energy development, gas-based industrialization, and institutional strengthening. These components must be implemented in a mutually reinforcing manner to fully harness the potential of the energy sector in the post-subsidy era.

➢ *Recommendations*

- *Enhance Domestic Refining Capacity through Continuous Investment*

Sustained investment should be directed toward improving domestic refining capabilities by rehabilitating existing facilities and promoting private-sector participation in refinery development. Encouraging both large-scale and

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modular refineries will help reduce reliance on imported petroleum products, ease pressure on foreign exchange, and improve national energy security.

- *Scale Up Renewable Energy Development, Especially Solar Power*

Nigeria should intensify efforts to harness its significant solar energy potential by expanding solar power infrastructure. This can be achieved through targeted incentives, improved access to financing, and the promotion of off-grid and decentralized energy solutions, particularly in rural communities, thereby improving energy access and supporting environmental sustainability.

- *Ensure Regulatory Stability to Attract Private Investment*

Establishing a consistent and transparent regulatory framework is critical for stimulating investment in the energy sector. Policymakers should focus on maintaining policy continuity, reducing uncertainty, and strengthening institutional effectiveness to foster investor confidence and encourage long-term participation.

- *Promote Gas-Based Industrialization as a Diversification Strategy*

Nigeria should capitalize on its abundant natural gas resources by advancing gas-driven industrial activities such as petrochemical production, fertilizer manufacturing, and gas-fired power generation. This approach will diversify the energy base, support industrial expansion, generate employment, and minimize gas flaring.

- *Expand Investment in Energy Infrastructure*

There is a need for substantial investment in energy infrastructure, including pipelines, storage facilities, and transmission systems. Strengthening these critical assets will enhance the efficiency of energy supply chains, reduce operational inefficiencies, and support the integration of both refined petroleum products and renewable energy sources.

Overall, the effective implementation of these policy measures will significantly enhance Nigeria's transition toward a more diversified, resilient, and sustainable energy system capable of supporting long-term economic development.

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