ANALYSIS OF KEY DETERMINANTS OF EXCHANGE RATE STABILITY IN NIGERIA

(1986-2018)

By

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This study analytically examines the key determinants of exchange rate stability in Nigeria which encompass GDP, Interest rate, Inflation rate, and Oil prices. Using annual data for the years 1986 to 2018. At the onset this study began its analysis by conducting descriptive statistics of the time series. The standard deviation indicates that exchange rate is more volatile than all the series followed by oil price. The skewness statistic reveals that only GDP was found to be negatively skewed all other variables remains positively skewed. The Jarque-Bera statistic indicates that Exchange rate, inflation rate and oil price were found to be normally distributed. Ramsey test affirms a linear relationship between exchange rate and GDP, Interest rate, Inflation rate, and Oil prices while the BDS test repudiate the claim and asserts that the relationship is nonlinear. The study in a bid to ascertain the true value of parameters employs both linear and nonlinear time series models to guide its analysis and empirical investigations. In the linear component, stationary analysis is performed by using ADF, PP and KPSS unit root test and the ARDL bounds testing approach for a long run relationship between the variables while in the nonlinear integral the KSS nonlinear unit root test and the NARDL bounds test was upheld. Bounds test established across the two models that long run relationship exist between exchange rate and its determinants. The empirical findings indicate that in the ARDL model the short run estimates revealed Oil price and GDP were found to be negatively related to exchange rate while Interest rate and inflation rate were found to be positively related to exchange rate, also the error correction term was found to be 57 %. In the NARDL cluster, where the impact of Oil Price was decomposed into positive and negative shock, the result reveals that positive oil price and GDP are negatively related to exchange rate, while the negative oil price shock, interest rate and inflation rate were positively related to exchange rate. Furthermore, CUSUM and CUSUMSQ tests reveals both models are dynamically stable. Finally, the study recommends that the Government should intensify efforts to revamp other sectors of the economy, embed them to a medium-long term diversification plan in order to improve foreign receipts which will consequently stabilize the exchange rate and mitigate the vulnerability and adverse effect of Oil price shock on exchange rate in Nigeria.