

# BACITI ECONOMIC INSIGHT

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Bashir Adeniji Center for International Trade and Investment



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The ongoing escalation of tensions involving the United States, Israel, and Iran in the Middle East has become one of the most important geopolitical developments shaping the global economy today. Unlike traditional wars confined geographically, this conflict has global implications due to the strategic importance of the Middle East in energy markets, global shipping routes, and financial systems. This insight examines the broader economic consequences of the conflict from the perspective of “bystander economies,” particularly Nigeria, where external shocks are transmitted

## **OPERATIONS EPIC FURY AND TRUE PROMISE 4: THE ECONOMIC COSTS FOR BYSTANDER ECONOMIES**

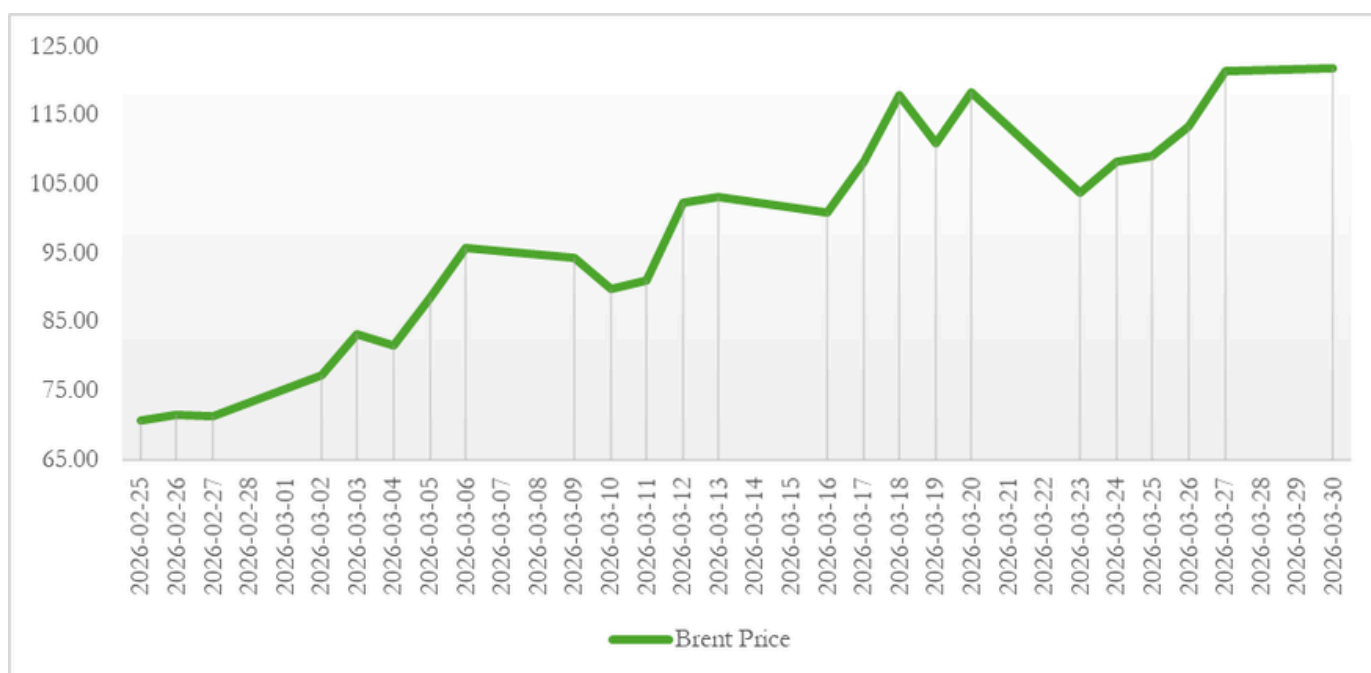


through oil price volatility, shipping disruptions, capital flow adjustments, and inflationary pressures. These channels affect price levels, exchange rates, and overall welfare, often amplifying existing structural vulnerabilities such as import dependence and weak industrial bases.

## Oil Price Trend recently

Starting at around \$70–72/pb in late February, prices were relatively stable, reflecting normal market conditions. The first decisive jump to about \$82–85/pb in early March signals the initial shock, where markets reacted quickly to the outbreak of conflict. As tensions intensified, prices surged further to around \$95/pb by March 6–7. This captures a phase of acute uncertainty where traders priced in worst-case supply risks. The mid-March peaks—climbing above \$110/pb and briefly approaching \$120/pb around March 18–21—represent the height of fear, likely driven by concerns over disruptions to critical shipping routes and potential escalation involving major oil transit corridors. Even when prices dip slightly afterward (around \$103–105/pb), they do not return to pre-conflict levels, indicating that uncertainty remains embedded. The final rise toward \$120 plus per barrel by the end of March shows a market that has fully internalized a persistent geopolitical risk premium. Now the US has signal to end the war even while still leaving the strait of Hormuz closed, it is expected that the market becomes less volatile in the coming period.

Figure 1: Oil Price trend



## Key Transmission Channels

### Oil Price Volatility

One of the most immediate transmission channels is energy price volatility. The tensions typically increase global oil prices due to fears of supply disruption. Since fuel is a major input in transportation, electricity generation and production, higher global oil prices quickly raise the cost of goods and services within Nigeria. This contributes to persistent inflationary pressure, especially in food and transport sectors. A particularly sensitive point in this system is the Strait of Hormuz, a narrow but critical maritime corridor through which approximately 20% of global oil trade passes daily. Any escalation involving Iran is especially important because Iran has historically had the capacity to disrupt or threaten passage through this route.

## How the Price Response Works

Several analyses indicate that oil prices tend to increase during geopolitical escalations due to two main mechanisms:

1. Supply uncertainty: Markets anticipate possible disruptions in production or shipping routes. So, when such disruptions are imminent, oil prices respond accordingly.
2. Risk premiums: Investors add a “geopolitical risk premium” to oil prices even when actual supply has not changed.

This means that oil prices can rise sharply without any physical shortage of crude oil, purely based on fear and uncertainty in global markets.

## Implications for Oil-Exporting Countries (Including Nigeria)

For oil exporters such as Nigeria, Angola, and Algeria, the impact is more complex and mixed.

### Positive side:

- Higher global oil prices increase export revenues.
- Governments earn more foreign exchange from crude oil sales.
- External reserves may temporarily improve.

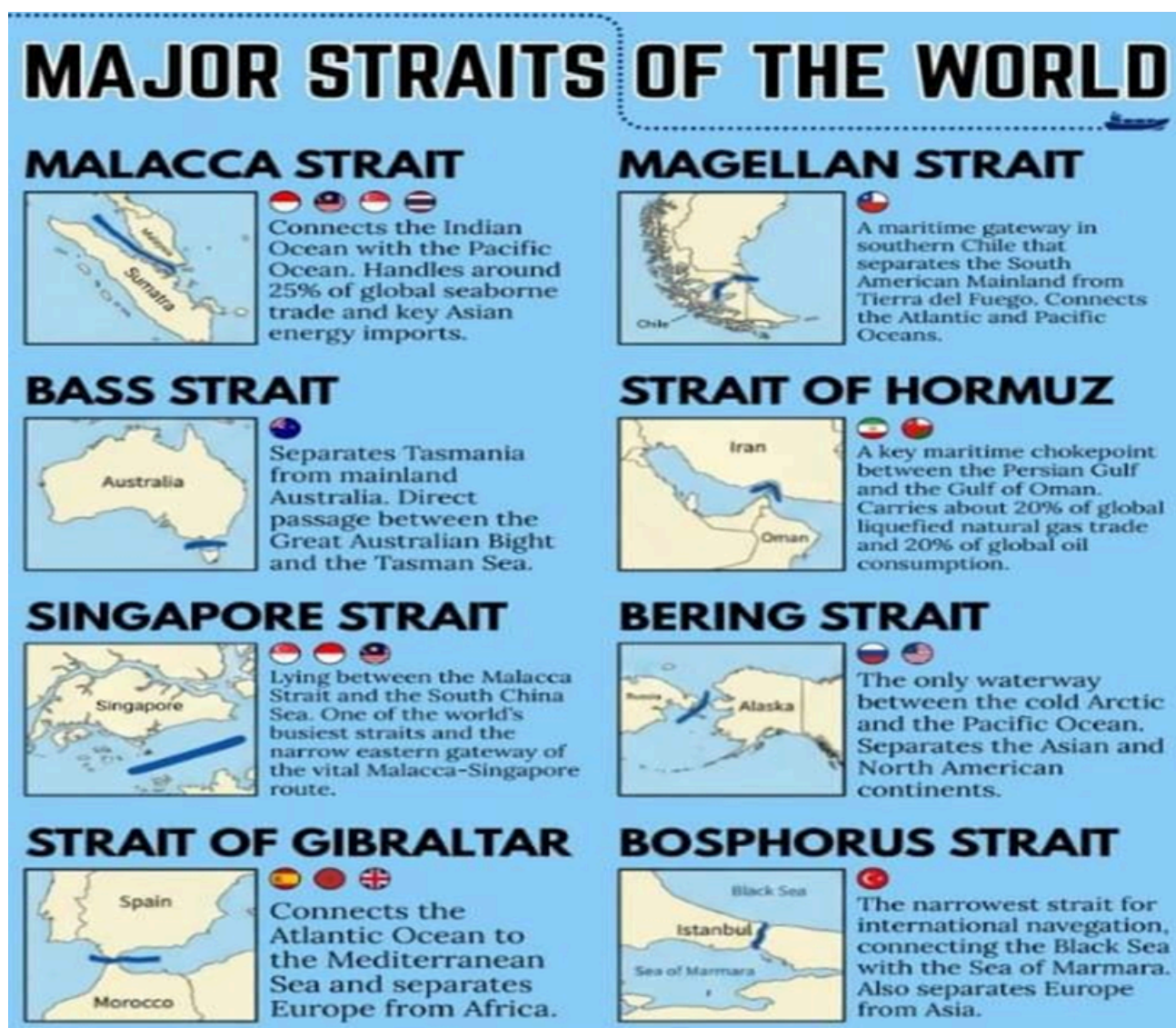
### Negative Side:

- Fuel price transmission: Even oil-producing countries like Nigeria import refined petroleum products. This means global price increases still raise domestic fuel costs. Even where local private refinery exists, the oil sale is still priced based on international price and high volume of its supply are from outside the country.
- Inflationary pressure: Higher transport and production costs feed into food and general inflation.
- Exchange rate volatility: Oil price spikes can strengthen external inflows, but instability in global markets can also increase currency volatility.

## Shipping and Trade Disruptions (Red Sea Crisis)

Beyond energy markets, one of the most immediate spillover effects of the U.S.-Israel-Iran tension in the Middle East has been the disruption of global maritime trade routes, particularly in the Red Sea corridor. This area has become increasingly unstable due to attacks on commercial vessels linked to broader regional conflict dynamics, raising serious concerns about the security of one of the world’s most important shipping lanes.

The Red Sea-Suez Canal route is a critical artery of global trade, connecting Asia, the Middle East, Africa and Europe. It is estimated that approximately 12-15% of global trade flows through this corridor. Any disruption in this route has immediate consequences for global supply chains, shipping costs and delivery timelines. As insecurity in the region has increased, many shipping companies have been forced to reroute vessels around the Cape of Good Hope in Southern Africa. While this alternative route avoids conflict zones, it is significantly longer, adding both time and cost to global shipping operations.



Source: Civixplorer

## Financial Market and Capital Flow Effects

In addition to trade disruptions, these geopolitical conflicts further have significant effects on global financial markets. These effects are primarily driven by rising uncertainty, which alters investor behavior and capital allocation across economies. During periods of geopolitical tension, global investors typically adopt a risk-averse stance, shifting capital away from emerging and developing markets toward safer assets.

## Poverty and Vulnerability

The welfare impact of global conflict is not evenly distributed across society. Instead, it disproportionately affects low-income and vulnerable households, deepening existing inequalities.

This happens for two main reasons:

- Higher expenditure share on essentials: Poor households spend a much larger proportion of their income on food, transportation, and energy. As a result, any increase in these prices has an immediate and severe impact on their welfare.
- Lack of savings buffers: Unlike wealthier households, low-income families often have little or no financial cushion to absorb sudden increases in living costs.

## Resulting Social Outcomes

These structural vulnerabilities lead to:

- Rising poverty rates, especially in urban informal settlements and rural communities.
- Increased food insecurity, as households struggle to afford basic nutrition.
- Greater reliance on informal coping mechanisms such as reduced meals, borrowing, or asset liquidation.

In this way, global geopolitical tensions translate into local human development challenges, particularly in food security and income stability.

## Policy Recommendations

The economic pressures arising from the U.S.-Israel-Iran conflict highlight the urgent need for both Nigeria and African economies to strengthen resilience against external shocks. While these shocks originate outside the continent, their impact is amplified by domestic structural weaknesses. Addressing these vulnerabilities requires targeted and coordinated policy responses.

### 1. Invest in Public Domestic Refining Capacity

One of Nigeria's most critical structural challenges is its dependence on imported refined petroleum products or private local refinery. This exposes the economy to global oil price volatility even as a crude oil exporter.

- Expanding domestic refining capacity would reduce reliance on imports.
- It would help stabilize domestic fuel prices.
- It would lower exposure to global supply disruptions and shipping costs.

### 2. Stabilize the Exchange Rate through FX Reforms

Exchange rate volatility remains a key channel through which global shocks affect the Nigerian economy.

- Strengthening foreign exchange market transparency and efficiency is crucial.
- Policies that boost non-oil export earnings can improve FX supply.
- Reducing market distortions and improving investor confidence can help stabilize the Naira.

A more stable exchange rate would reduce imported inflation and improve macroeconomic predictability.

### 3. Strengthen Agriculture and Food Systems

Food inflation is one of the most significant drivers of cost-of-living pressures in Nigeria.

- Investing in agricultural productivity can reduce dependence on food imports.
- Improving storage, logistics, and rural infrastructure can lower distribution costs.
- Supporting farmers with inputs and financing can increase domestic supply.

A stronger agricultural sector would enhance food security and reduce vulnerability to global price shocks.

### 4. Expand Social Protection Programs

Given the significant welfare impact of rising inflation, there is a need to strengthen support systems for vulnerable populations.

- Expanding targeted cash transfer programs can cushion low-income households.
- Investing in social safety nets can reduce the impact of economic shocks.
- Improving the efficiency and coverage of welfare programs is critical.

## Conclusion

The ongoing U.S./Israel-Middle East conflict has significant economic consequences for Nigeria and African economies. Through oil price shocks, trade disruptions, and financial volatility, the conflict has: Increased inflation; Weakened exchange rates; Reduced welfare; Slowed economic growth. Ultimately, the crisis highlights the structural fragility of African economies and the urgent need for economic diversification and policy reform.