



EXCHANGE RATE DYNAMICS AND BALANCE OF PAYMENTS PERFORMANCE IN NIGERIA: EVIDENCE FROM AN ARDL APPROACH

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ABSTRACT

This study examines the dynamic relationship between exchange rate movements and balance of payments performance in Nigeria from 1975 to 2024, a period marked by major structural changes, global shocks, and shifts in exchange rate policies. Anchored on the Elasticity Theory of the Balance of Payments and is founded on the idea that nominal exchange rate, inflation rate and interest rate and trade openness are incorporated into an autoregressive distributed lag (ARDL) framework to capture both the short-run and long-run dynamics. The sources of annual time-series data were the Central Bank of Nigeria (CBN) and the National Bureau of Statistics (NBS). The results indicate that there is a statistically significant co-integration of the variables in the long-run. In particular, exchange rate and trade openness have positive and significant impact on the balance of payments and inflation has negative impact reflecting its distortionary impact on the competitiveness of the exports. Interest rate also causes a positive contribution to the external balances through its contribution to attract capital inflows. The findings are that the external sector adjustments of Nigeria are very sensitive to changes in the exchange rates and macroeconomic fundamentals. The study concludes that steady management of the exchange rates coupled with the diversification of trade and the inflation indexation is paramount in restoring the external balance of Nigeria and leading to long term macroeconomic growth.

Keywords:

Exchange Rate, Balance of Payments, Trade Openness, Inflation, Interest Rate

1.0 Introduction

The process of international trade, financial flows, and foreign direct investment has made the issues of national economies more and more interdependent making exchange-rate management a focus among policy-makers, particularly in the developing world (Ibarra & Blecker, 2014; Huchet-Bourdon and Korinek, 2011). The exchange rate is one of the important price mechanisms that connects the domestic economy with the international one, affecting inflation, capital movements, international competitiveness of exports, demand of imports, and reserve levels (Agundu, Akani, and Kpakol, 2013). In

the same vein, balance of payment (BOP) refers to a full account of the economic activities of a country with the outside world, it is an important indicator of performance on an external sector (Imoisi, 2012). The long-term imbalance in the BOP may lead to a change in the exchange rates, exhaust foreign reserves, and make it harder to plan in terms of macroeconomic activity, especially in economies that are dependent on resources (Odili, 2014).

Nigeria has been experiencing the crises of external stability since 1975 in the

management of exchange-rate fluctuations. The naira was quite stable throughout a regime that was fixed and determined by various administrators until opening the Structural Adjustment Programme (SAP) in 1986 (Ismaila, 2016). Nevertheless, the drop in oil prices, the increase in the demand of imports, and the continuing negative balance of payment revealed the existence of severe structural defects in the economy (Nwanosike, Uzochina, Ebenyi, & Ishiwu, 2017). In its reaction, Nigeria implemented a succession of market-based exchange-rate regimes, such as the Second-Tier Foreign Exchange Market (SFEM) in 1986, the Dutch Auction System (DAS) in 2002, the Inter-Bank Foreign Exchange Market (IFEM) in 1999, and Investors/Exporters (I&E) window in 2017 (Central Bank of Nigeria [CBN], 2023). These reforms notwithstanding, the naira has not been stable because of the excessive reliance of the country on crude-oil export, poor performance of the non-oil exports, the pressures of capital-flight, and the high propensity to importation (Odili, 2014; Agundu et al., 2013).

Global and domestic shocks over the last few years have further redefined the dynamics of the external sector of Nigeria. The oil-price crash of 2014-2016 and the 2020 coronavirus epidemic, as well as the foreign-exchange harmonisation reform of 2023, have heightened the vulnerability of the external sector (World Bank, 2024; CBN, 2023). These shocks were further added to by the fact that fuel subsidies went away and that inflation was worsened, which hit over 27 percent in late 2023 (National Bureau of Statistics [NBS], 2024). At the same time, the depletion of the foreign reserves, the depreciation of the exchange rates, and the constant trade deficits undercut the external stability of Nigeria. Despite a temporary surplus in the current account in the period between 2015 and 2024, imports still outweighed non-oil exports, which indicates the presence of structural imbalances (CBN, 2024).

What these developments highlight is the intricate interaction of the economic fundamentals and political influence in advancing the relationship between exchange rate and the BOP in Nigeria. This nexus is important to understand in order to design the sustainable macroeconomic and exchange-rate policies that can achieve the external balance and promote long-term growth. Even though many studies have been conducted on the effects of exchange-rate changes on the external sector of Nigeria, most have analyzed the effect of isolated variables, including the trade balance, current account, or capital flows instead of the overall balance of payments (Eke, Eke, and Obafemi, 2015; Delimus, Obumneke, and Muhammed, 2018; Abdullahi, Abubarkar, Fakunmoju, and Giwa, 2016). There is very little empirical information that tests the overall balance of payment in terms of long-term analysis found in Nigeria. Numerous studies utilize brief periods of time or end before major structural and policy shocks. As an illustration, Oladipupo and Ogebenovo (2011) and Agundu et al. (2013) discussed the data as of the middle of the 2010s, whereas Oladipupo (2014) only up to 2012. It is clear that the small amount of research that has made use of post-2018 data is insufficient because it would include recent destabilizing events that include the COVID-19 pandemic, the 2023 exchange-rate unification reform, and the increase in external-debt service burden (CBN, 2023; World Bank, 2024).

In the global context, long-horizon studies that explore the entire structure of the balance of payments including the current, capital and financial accounts are also not common with most empirical literature concentrating on the dynamics in trade-balance as well as current-account adjustments (Stucka, 2004; Gligoric, 2010; Masoom, Bhat, Arshad, and Chaman, 2025). Most of them are based on short periods even the ones who adopt a holistic approach, or they do not consider the complex interrelationship between inflation, trade openness, and exchange-rate policy (Ibarra

and Blecker, 2014; Ribeiro, Lima, and McCombie, 2014). There still therefore seems to be a gap in the literature on the relationship between Nigeria exchange rate and BOP with respect to recent macroeconomic reforms and external-sector adjustments.

To overcome these gaps, the paper reevaluates the dynamic relationship between exchange rate movements and balance of payments performance in Nigeria with reference to the yearly data between the period of 1975 and 2024. This is the time of major shifts in policies, economic crises and structural changes which have determined the external sector in the country. Using Autoregressive Distributed Lag (ARDL) framework, the paper will determine the short-run and long-run impacts of the exchange-rate dynamics, trade openness, interest rate, and inflation on BOP of Nigeria. It is hoped that the findings will give evidence-based contributions to better exchange-rate management, policy in trade, and enhancement of external-sector stability to enhance the sustainable economic growth.

2.0 Literature Review

The exchange rate is a price of a specific currency in relation to the other, whereas the balance of payments (BOP) is an international financial transaction and a trade position of a country with the rest of the world (Imoisi, 2012). The exchange rate should be well managed as it helps in promoting macroeconomic stability and sustainable growth since the exchange rate changes also have a lot of impacts on other major macroeconomic variables including inflation, interest rate, money supply, trade balance, and the overall balance of payment. The exchange-rate management issue is of significant concern to policy makers since no nation exists in isolation and there is the aspiration of every nation to have a balance in its balance of payments.

2.1 Elasticity Theory of the Balance of Payments.

Elasticity Theory of the Balance of Payments is the sophisticated theory that was created by Robinson (1937) and then furthered by the Marshall-Lerner condition that demonstrates how the exchange rate variations can influence the external balance of a country by impacting on exports and imports (Husted and Melvin, 2013). The theory argues that exporting of goods becomes cheaper and the importation of goods is costlier by way of currency depreciation. When the sum of price elasticity of the demand of exports and imports is greater than one, the balance of trade and therefore the balance of payments will be improved (Ibarra & Blecker, 2014).

The exchange rate in the context of Nigeria has a direct effect on the external competitiveness and the capacity of foreign earnings. Nevertheless, the elasticity of trade to the exchange-rate movements has been poor in general due to the heavy reliance of the country on crude-oil exports and an import-based structure of production, which has led to constant deficits in balance-of-payment (Odili, 2014; Nwanosike, Uzoechina, Ebenyi, and Ishiwu, 2017). This mechanism is in interaction with other macro variable: inflation undermines export competitiveness through increasing domestic prices (Huchet-Bourdon and Korinek, 2011); interest rate is a factor of capital flows that impact the financial account of the BOP (Masoom, Bhat, Arshad, and Chaman, 2025); the responsiveness of exports and imports to exchange-rate fluctuations depends on trade openness (Agundu, Akani, and Kpakol, 2013). In this regard, using the elasticity theory, there is a theoretical basis of association between exchange rate, inflation, interest rate, and trade openness with the balance-of-payments performance. It describes the transmission of exchange-rate variations both in the trade and financial channels to affect external-sector outcomes.

2.2 Empirical Review

Empirical research has yielded both inconclusive results on the association between exchange rate and balance-of-payments performance between various economies. Stucka (2004) used a reduced-form model to quantify the response of the balance of trade to a permanent depreciation of the domestic currency in Croatia to assess the implications of variation of the exchange rate on the balance of trade. The results showed that an increase in depreciation by 1 percent has a positive effect on the equilibrium trade balance by 0.94 to 1.3 percent, and a new equilibrium was reached in about 2.5 years which proved the J-curve effect. Equally, Gligoric (2010) examined the relationship between exchange-rate and trade and balance of payments in Serbia under both the Johansen and ARDL models and found out that the trade balance was enhanced by the real exchange-rate depreciation.

In the present study, Masoom, Bhat, Arshad and Chaman (2025) investigated the effect of exchange rate on current account balance through ARDL and Granger causality models, which revealed a significant positive effect of the exchange rate on current account balance. Oladipupo (2020) and Abdullahi (2019) used the Ordinary Least Squares (OLS) and Granger causality models to determine the causality of exchange rate on the current account balance in Nigeria. They discovered that the exchange rate as well as money supply had a positive effect on the balance of current account in Nigeria whereas money supply, GDP, consumer price index and interest rate had weak and negative effects.

On the other hand, Ahmad and Jimi (2019) discovered that exchange-rate instability had a negative impact on the current-account balance of Pakistan. Ahmad et al. (2019) also examined the association between currency rates and the BOP in Pakistan by applying the ARDL and Granger causality tests and concluded that exchange-rates stability

increases investment and balance of payment.

A similar study done by Delimus et al. (2018) using the ARDL method to analyse the effect of exchange rate on the BOP (1999-2016) capital and financial account showed that the nominal exchange rate positively affected the capital and financial account of Nigeria significantly. On the other hand, a significant negative association was found between exchange rate and the capital account of the BOP (1986-2014) according to the ADF, Johansen co-integration, and ECM methods (Eke et al. 2015). According to Odili (2014), an experiment on annual data (1971-2012) using ARDL showed that the long-run relationship between exchange rate and BOP was positive and significant, whereas the short-run relationship was of positive but insignificant effect.

Eke et al. (2015) also tested the impact of exchange rate on the balance of trade in Nigeria (1970-2012) and determined that it makes a significant negative impact and Shafi et al. (2015) tested the effect of exchange rate, inflation, and interest rate on the BOP of India and Pakistan, which were found to have a positive impact on the former and negative impact on the latter. The OLS and Granger causality analysis of the Nigeria (1970-2014) revealed that exchange rate and money supply remarkably enhanced the BOP, as compared to the money supply, GDP, CPI, and interest rate, which had a negligible negative impact on the BOP (Abdullahi et al., 2016).

3.0 Methodology

This study employed a quantitative research design, collecting annual time-series data to examine the dynamic relationship between exchange rate movements and balance of payments performance in Nigeria from 1975 to 2024. The balance of payments functions as the dependent variable, quantified as the aggregate net external transactions including the current, capital, and financial accounts, articulated in U.S. dollars and

sourced from the Central Bank of Nigeria (CBN) Statistical Bulletin (2024). The primary explanatory variable in the analysis is the nominal exchange rate, quantified as the annual average value of the naira relative to the U.S. dollar, sourced from the Central Bank of Nigeria Statistical Bulletin (2024). This measure was favoured as it accurately represents market and policy-induced fluctuations in Nigeria's exchange rate over time, aligning with previous research on exchange-rate and balance-of-payments dynamics (Odili, 2014; Agundu, Akani, & Kpakol, 2013). The inflation rate (INF) is quantified as the annual percentage variation in the Consumer Price Index (CPI) from the National Bureau of Statistics (NBS, 2024), indicating domestic price volatility that may undermine export competitiveness. The interest rate (INT) represents the average yearly loan rate, reflecting the cost of borrowing and its impact on capital flows, derived from the CBN Statistical Bulletin (2024). Commerce openness (TOP) is determined by the ratio of total commerce (exports plus imports) to gross domestic product (GDP), multiplied by 100, derived from data provided by the CBN and World Bank (2024), reflecting Nigeria's engagement in global trade.

3.1 Model Specification

This study is based on the elasticity theory, which shows what happens to trade balance when a country devalues its currency and conditions that must prevail in the foreign exchange market for a devaluation or

depreciation of the currency to improve the trade balance and balance of payment. The model of Odili (2014) which is given as: $BOP = f(EXR, XM, IM)$ was adapted in this study. Where: BOP is Balance of payment, EXR is exchange rate, XM is total export, IM is total import. However, by modification, trade openness is added in this study to capture the level of openness of the country to international trade which determines the level of exchange rate through the demand and supply of currency while Interest Rate and inflation rate are adopted as control variable. Thus, the model for this study is given as:

$$BOP = f(EXR, INF, INT, TOP) \quad (1)$$

All variables were converted to their natural logarithmic forms to stabilise variance and facilitate elasticity-based interpretation. Nevertheless, due to the BOP variable potentially containing both positive and negative values, a logarithmic transformation was carried out with a modified method to account for negative entries, as expressed in the following manner:

$$\ln BOP = \ln(|BOP| + 1) \times \text{sign}(BOP) \quad (2)$$

This approach retains the direction of balance-of-payments values (surplus or deficit) while allowing for valid logarithmic transformation and statistical stability.

While the Econometrical model is given as:

$$\ln Bop = \beta_0 + \beta_1 \ln EXR + \beta_2 \ln INF + \beta_3 \ln INT + \beta_4 \ln TOP + \mu_t \quad (3)$$

Where:

BOP = Balance of Payments
 EXR = Exchange Rate
 INF = Inflation Rates
 INT = Interest Rate
 TOP = Trade Openness
 β 's = Coefficients of the variables to be estimated.

Ln = natural log notation

3.2 Data Estimation Techniques

This study utilized the Autoregressive Distributed Lag (ARDL) model to analyse the short-run and long-run impacts of exchange rate, trade openness, money supply, and inflation rate on Nigeria's balance of payments. The ARDL

methodology, formulated by Pesaran, Shin, and Smith (2001), is appropriate for time-series data exhibiting mixed integration orders, where variables are stationary at level I(0) or at first difference I(1), but not at second difference I(2). Before estimate, all variables underwent the Augmented Dickey-Fuller (ADF) unit root test to assess their stationarity characteristics. The Bounds co-integration test was subsequently employed to ascertain the presence of a long-term link among the variables. Following the establishment of co-integration, the ARDL model was calculated to elucidate both the short-run dynamic adjustments and long-run equilibrium linkages between the exchange rate and balance-of-payments performance. To guarantee the robustness and reproducibility of the findings, a set of post-estimation diagnostic assessments were

performed. The Breusch-Godfrey Serial Correlation LM Test evaluates serial correlation, the Breusch-Pagan-Godfrey Test examines heteroskedasticity, the Jarque-Bera Test assesses normalcy, and the Ramsey RESET Test evaluates model stability and specification accuracy. The ARDL framework was favoured due to its adaptability with small sample sizes, its capacity to concurrently estimate short-run and long-run effects, and its resilience to endogeneity issues among regressors.

The research employed the Autoregressive Distributed Lag (ARDL) model to test the existence of long run relationship among the variables (Pesaran et al., 1999, 2001; Wolde-Rufael, 2010). The model is expressed in the equation below:

$$\Delta \ln BOP_t = \beta_0 + \sum_{i=1}^n \beta_{1i} \Delta \ln BOP_{t-i} + \sum_{i=m}^n \beta_{2i} \Delta \ln EXT_{t-i} + \sum_{i=m}^n \beta_{3i} \Delta \ln INF_{t-i} + \sum_{i=m}^n \beta_{4i} \Delta \ln INT_{t-i} + \sum_{i=m}^n \beta_{5i} \Delta \ln TOP_{t-i} + \mu_t \tag{4}$$

Where; Δ is the first difference operator, β_0 is the drift component and μ_t is the white noise error term. The equation above connotes the term with the summation sign represents the error correction dynamics i.e. β_{1-5} represents the long-run relationship.

Where:

- H0 is null hypothesis (no long run relationship)
- H1 is alternative hypothesis (long run relationship exists)

If co-integration is identified in the model, the short run equation to estimate the model will be as follows (Pesaran et al., 2001; Wolde-Rufael, 2010)

$$\Delta \ln BOP_t = \beta_0 + \sum_{i=1}^n \beta_{1i} \Delta \ln BOP_{t-i} + \sum_{i=m}^n \beta_{2i} \Delta \ln EXT_{t-i} + \sum_{i=m}^n \beta_{3i} \Delta \ln INF_{t-i} + \sum_{i=m}^n \beta_{4i} \Delta \ln INT_{t-i} + \sum_{i=m}^n \beta_{5i} \Delta \ln TOP_{t-i} + \delta EMC_{t-1} + \mu_t \tag{5}$$

Where: *ECM* is the error correction term which is the residuals retrieved from the estimated long-run relationship.

Equation (3) is the ARDL short run specification; it is derived through the construction of an error correction model (ECM). The coefficient of the ECM represents the speed of adjustment to

equilibrium position whenever there is deviation as a result of shocks, thus it must be negative and significant. The ECM is therefore the error correction term and is lagged by one period to show the percentage of its speed of adjustment from a shock in the previous period to equilibrium in the current period. All coefficients in equation (3)

reveals the short run impact of the independent variables on $\Delta \ln BOP_t$, hence, the first difference operator Δ .

4.0 Results and Discussion

4.1 Unit Root test

Table 1: Augmented Dickey-Fuller (ADF) Unit Root Test

Variable	ADF t-Statistic value	5% Critical Value	Prob 5%	Order of Integration
LnBOP	6.336685	2.9350	0.0000	I(1)
LnEXR	4.313352	2.9297	0.0013	I(1)
LnTOP	5.269461	2.9281	0.0001	I(1)
INF	3.778633	2.9297	0.0060	I(0)
INT	7.382555	2.9297	0.0000	I(1)

Source: Researcher's computation (2025)

Table 1 result shows that Inflation Rate is stationary at levels. That is, the ADF T-statistic value is greater than the critical value at 5% level of significance. Whereas, that of Interest Rate, Balance of payment, Exchange rate, Trade Openness is seen to be stationary at first difference I(1). However,

since the macroeconomic variables employed are mixture of I(0) and I(1) variables, the study employs the Autoregressive Distributed Lag – Bound Co-integration technique of short run and long run equilibrium.

4.2 Bound Test of Cointegration

Table 2: Bound Test Result

F-statistic	K	1%		5%		10%	
		Lower bound	Upper bound	Lower bound	Upper bound	Lower bound	Upper bound
6.095606	3	3.65	4.66	2.79	3.67	2.37	3.20

Source: Researcher's computation (2025)

Given the result of the Bound Test, the F-statistic value should be compared with the Pesaran critical value at traditional levels of significance. From the result in table 2, the F-statistic 6.095606, is greater than the upper bound critical value at 5% level of significance (4.01), we thus reject the null hypothesis of no long run relationship and conclude that there is a long-run co-integrating relationship existing among the variables considered in this study. Thus,

implying that exchange rate, Interest and Inflation Rate are good determinants of balance of payments in Nigeria. From the result, we can hence estimate both the short-run and the long run relationship between independent variables and the explanatory variables selected for the study.

4.3 Autoregressive Distributed Lag estimation

Having identified the existence of a long run relationship between variables of interest whose order of integration have been determined, in this section, an error

correction model is formulated. The error correction model represents an alternative way of presenting long run equilibrium relationship between variables. It shows the dynamic error term analysis of the co-integrated variables (Madichie & Maduka 2014).

Table 3: ARDL Short-Run Coefficients Regression result

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(LNEXR)	-0.152127	0.124114	-0.419995	0.0341
D(LNTOP)	2.943699	1.040462	2.829223	0.0078
D(LNTOP(-1))	-1.374103	1.035350	-1.327186	0.1933
D(LNTOP(-2))	-3.884950	0.922385	-4.211854	0.0002
D(INF)	-0.493119	0.178528	-2.762142	0.0092
D(INT)	1.838492	0.829869	2.215401	0.0335
ECT(-1)	-0.891907	0.168699	-5.286964	0.0000

Source: Researcher’s computation (2025)

The ECT coefficient shows how quickly variables converge to equilibrium and it should have a statistically significant coefficient with a negative sign. The result of short run ARDL is presented in Table 3. The Error Correction Term reveals that there is speed of adjustment among the macroeconomic variables with a negative value of -0.891907 and significant value of 0.0000. This implies that there is a high speed of adjustment from the short run to long run; if there’s any disequilibrium/ deviation in the system, it takes an average speed of 89% to adjust back from the short to the long run. Meaning that balance of payments will adjust back to equilibrium at speed of 89% annually.

negative and significant effect on balance of payments. Moreover, the result shows that trade openness and Interest rate exerts positive and significant effect on balance of payments. This implies that a fall in the Exchange Rate of the Naira (Depreciation) in relation to the U.S. dollars (Appreciation) increases the Balance of Payments. This may be attributed to the demand elasticity of our exports, which are mostly primary products such as crude oil and cash crops. This view is supported by Jhigan (2006), who opined that for Balance of Payments deficits to be reduced in most third world countries, their currencies should be depreciated because most of their exports are primary product which have elastic demand in the international market.

Also, in the short run it is revealed that exchange rate and Inflation rate both have

Table 4. ARDL Long-Run Coefficients Regression result

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LNEXR	0.357335	0.030971	-0.559705	0.0193
LNTOP	2.278190	2.623374	0.868420	0.0413
INF	-0.609339	0.253776	-2.401095	0.0220
INT	1.290559	0.627426	2.056909	0.0474
C	-2.043453	9.579789	-0.213309	0.8324
LNEXR	0.357335	0.030971	-0.559705	0.0193

Source: Researcher’s computation (2025)

Table 4 above indicates the long run equilibrium relationship, the result reveals that in the long run, exchange rate has positive and significant effect on balance of payments with coefficient of 0.357335 which implies that a percentage increase in exchange rate will lead to 35.7% increase in balance of payments. This could be as a result of increase in the importation of finished goods and services in Nigeria due to inefficiency and ineffectiveness of the manufacturing industry which led to increase in the Inflation rate. Furthermore, the result shows that Interest Rate has coefficient of 1.290559 which is significant at 5% indicating that a percentage increase in Interest Rate will lead to 129.05% increase in

balance of payments in Nigeria. The result also shows that Trade Openness has coefficient of 2.278190 which is significant at 5% indicating that a percentage increase in Trade Openness will lead to 227.81% increase in balance of payments in Nigeria. Also, the result indicates that there is negative and significant relationship between Inflation rate and balance of payments with coefficient of -0.609339 and insignificant at 5% indicating that a percentage increase in Inflation will lead to 60% decrease in balance of payments in Nigeria. A rising inflation rate reduces overall national output which in turn drastic trigger fall in export.

4.4 Diagnostic Tests

Table 5. Breusch-Godfrey Serial Correlation LM Test:

F-statistic	2.190186	Prob. F(1,39)	0.1469
Obs*R-squared	2.392764	Prob. Chi-Square(1)	0.1219

Source: Researcher's computation using Eviews 9

Autocorrelation implies that the residuals of the model are correlated. The Breusch-Godfrey Serial Correlation LM Test result reported in Table 5 indicates the absence of serial correlation in the

regression's residual with probability value of 0.1469 which is greater than 0.05 significant level.

Table 6. Heteroskedasticity Test: Breusch-Pagan-Godfrey

F-statistic	0.600026	Prob. F(4,40)	0.6648
Obs*R-squared	2.547275	Prob. Chi-Square(4)	0.6362
Scaled explained SS	1.574562	Prob. Chi-Square(4)	0.8134

Source: Researcher's computation using Eviews 9

The result of the Heteroskedasticity presented in Table 6 indicates that the residual is Homoscedastic as indicated by the probability value of Breusch-Pagan-Godfrey test. The Breusch-Godfrey test for autocorrelation and heteroskedasticity

shows the absence of autocorrelation and heteroskedasticity in the model, as the probability value of the F-statistic is insignificant, which thus lay credence to the reliability of the ARDL model specified as well as the outcome the study arrived at.

Table 7. Ramsey RESET Test

	Value	df	Probability
t-statistic	1.115571	39	0.2709
F-statistic	1.244498	(1, 39)	0.2709

Source: Researcher's computation using Eviews 9

The Ramsey Reset stability test presented in table 7 shows that there are no omitted variables in the model and the model is relatively stable given a probability value of 0.2709 which is greater than 0.05.

5.0 Conclusion

Exchange rate is the price of a country's currency in relation to foreign currencies. Exchange rate serves as one of the major macroeconomic variables that affect the trade positions of a country and ultimately balance of payments. The need for effectively managed exchange rate system is emphasized due to the harmful effect of unstable exchange rate on economic performance. This study thus explored the effect of exchange rate on overall balance of payments in Nigeria. It was established that exchange rate which has been relatively stable recently promote balance of payments in Nigeria. The implications of this result is that a stable exchange rate would strengthen the value of local currency, promote exportation of local goods, makes the importation of foreign goods dearer and enhances domestic investment and foreign investment which ultimately contribute positively to balance of payments. It is thus concluded that exchange rate stability has the capacity to adjust balance of payments deficit. Thus, it was recommended that the current exchange rate regime employed by the monetary authority should be sustained. Exchange rate stability should be pursued vigorously because internal and external performance of the nation hovers around exchange rate stability. Government should ensure the effective and efficient management of the exchange rate in order to reduce exchange rate fluctuation and instability. Government should embark on policies that would make trade openness work in favor of Nigeria through the diversification of the economy to other sectors like agriculture, tourism and manufacturing amongst others.

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