

Economic Report | Monthly Update

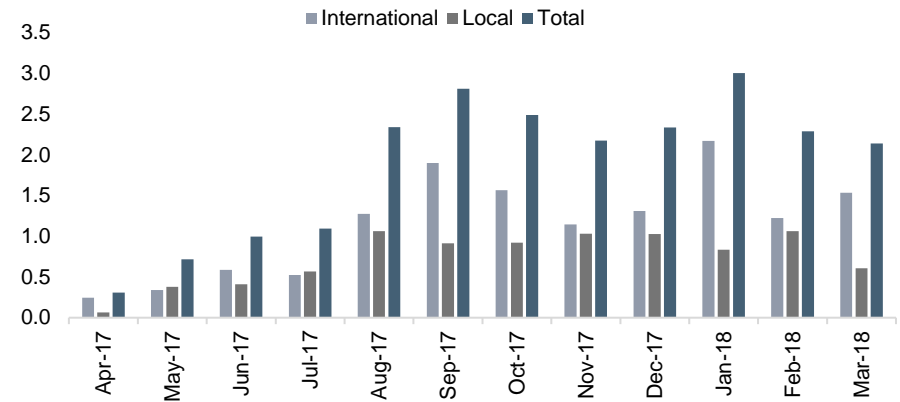
Economic Update – March 2018

Declining FPI, improved FDI!

In the month of March, net-supply at the Investors and Exporters Window (IEW) rose 25% MoM to \$168 million compared to \$134 million recorded in February. The increase stemmed from a 16% jump in aggregate sales. Going by breakdown, international inflows at the IEW rose by 25% MoM to \$1.5 billion (\$1.2 billion in February) reflecting a strong rebound in FDI (+87% MoM to \$122 million) and Other corporates (+862% MoM to \$300 million) which more than offset slight decline in FPI (-1.3% MoM to \$1.1 billion). Aggregate local inflow dipped 43% MoM to \$605 million due to a 20% MoM decline in CBN supply to \$145 million, its lowest level in three months, which was further amplified by lower sales from Exporters and Other corporates with a combined decline of 47% MoM to \$458 million. Consequently, overall inflow at the IEW printed at \$2.14 billion (February: \$2.28 billion).

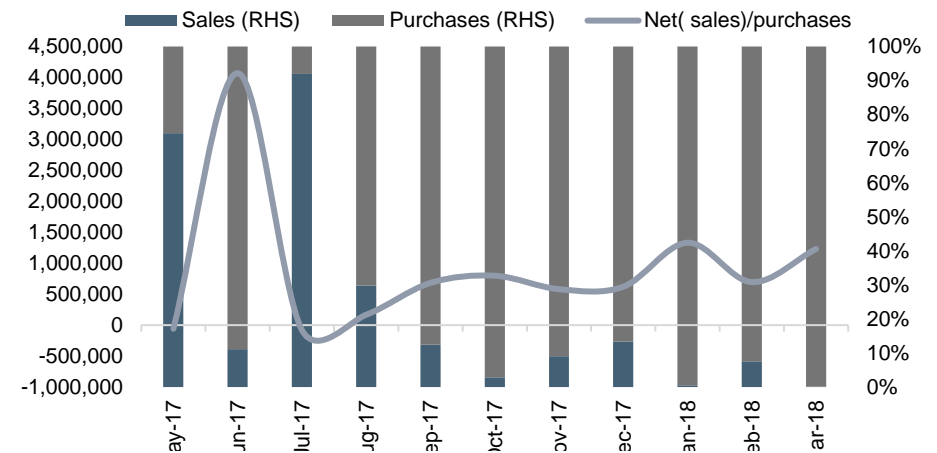
In a deviation from the previous month, the demand picture changed in March with a 15% increase in purchases to \$2.1 billion (February: \$1.78 billion). Notably, the higher demand stemmed from a rebound in CBN purchases at the window, which rose 63% MoM to \$1.2 billion to account for 59% of total purchases at the window. The consistently supply-demand gap at the IEW has provided the CBN an easy avenue to shore up its reserves (+8.9% MoM to \$46 billion) to ensure currency stability.

Figure 1: FX Inflow at the I&E Window (\$'Billion)



Source: FMDQ, ARM Research

Figure 2: CBN Activity at the IEW (\$'000) vs. Balance (\$'billion)

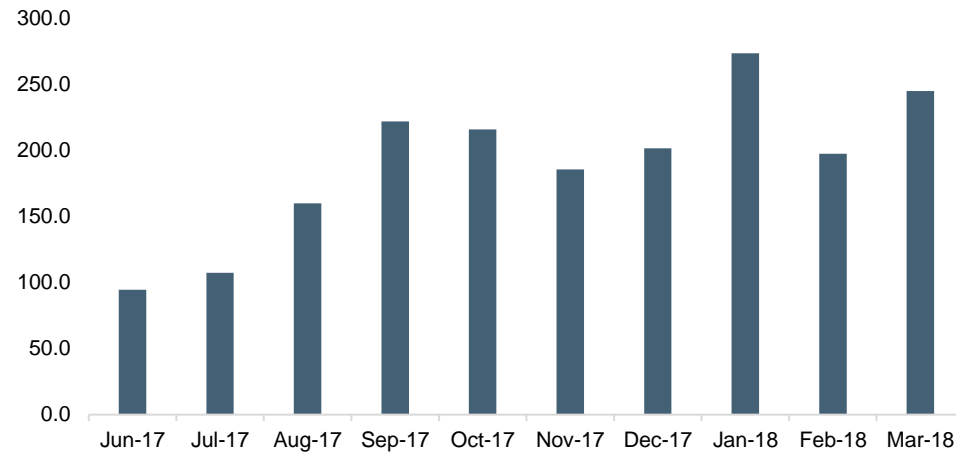


Source: FMDQ, ARM Research *Data estimated using monthly avg. exchange rate at the IEW*

Reflecting a rebound in market activity during the month, daily average turnover rose 24% MoM to \$245 million, with corresponding total transaction rising 30% MoM to ~\$5.1 billion – 37% of the total transaction consummated between the range of ₦340-359/\$. The relative stability of the naira persisted across segments of the foreign exchange market. At the parallel market, transactions were consummated at an average rate of ₦361/\$ (+0.14% MoM appreciation versus +0.25% in February) as the apex bank aggressive sales persisted at the SMIS wholesale, SMEs and Retail invisibles segments. Elsewhere, the NAFEX and BDC rates were relatively flat, closing at ₦360.13/\$ and ₦360.87/\$ which is lower 0.02% and 0.07% MoM respectively.

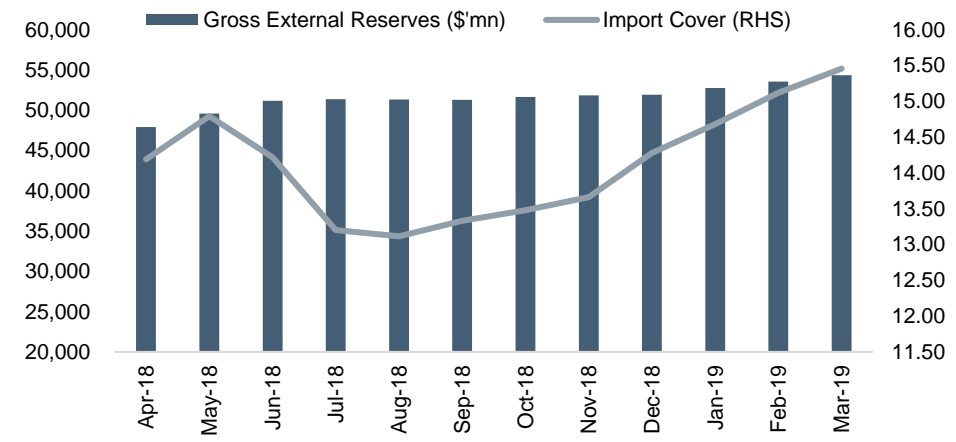
Going forward, with our forecast monthly crude oil (\$1.3 billion) and non-oil (\$2.4 billion) inflows as well as our position on foreign portfolio flows, we do not foresee any sudden shock to the currency as the apex bank is well positioned to continue its aggressive dollar sale across segments of the window. Thus, with our forecast average monthly CBN outflow of \$3.1 billion in total at different segments of the FX market and possible outflows via maturing money market instruments by foreign investors (30% of total maturing bills estimated at \$9.5 billion), we believe the reserves will end the year above \$50 billion with an import cover in excess of 14 months.

Figure 3: Avg. IEW FX Intervention (\$'million)



Source: FMDQ, ARM Research

Figure 4: Forecast movement in gross reserves and import cover (\$'million)



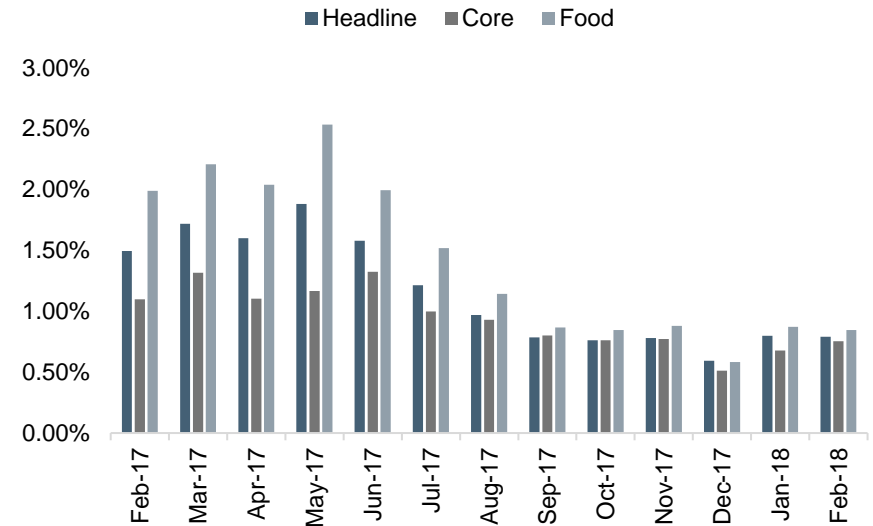
Source: CBN, ARM Research

Inflation fast-tracks its descent in February

In our recent commentaries, we had explained that headline inflation is set to extend its downtrend in 2018 helped by favorable base effects in 2017 which were particularly strong in H1 17. In line with our prognosis, despite a modest 1bp decline in MoM inflation, headline inflation for the month of February dipped 80bps to 14.3% from 15.3% in the month of January. Elevated food prices presented the high base with February 2017 food inflation at 18.5% (versus 5-year average of 10.1%) owing to increased export of grains to neighbouring countries following the devaluation of the currency – which also had a negative impact on imported food. In recent months, food prices have moderated, induced by sufficient market supplies from the ongoing dry season harvest. Consequently YoY food inflation dipped 133bps to 17.6% while MoM food inflation dipped 3bps to 0.85% in the review month.

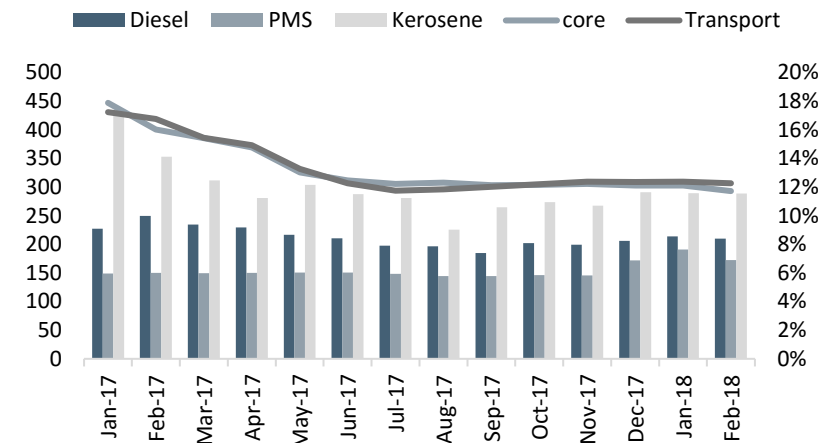
Similarly, core inflation declined 38bps to 11.7% in February despite an 8bps increase in MoM core inflation to 0.75% – also driven by favourable base effects. The increase in MoM inflation stemmed from jumps in Alcoholic Beverage (13bps), Communication (+9bps) and Clothing, Footwear & Health (7bps). During the month, energy prices moderated across board (PMS: -9.6% MoM, Diesel: -1.8% MoM, Kerosene: -0.1% MoM and Cooking Gas: -1.6% MoM) with PMS declining the most following improved domestic supply of petrol by the NNPC around the country. Despite this, the Housing Water Electricity Gas & other Fuels (HWEGF) division rose 3bps to 0.62% MoM although, the scale of uptick was slower than 15bps in the prior month.

Figure 5: Trend in MoM inflation



Source: NBS, ARM Research

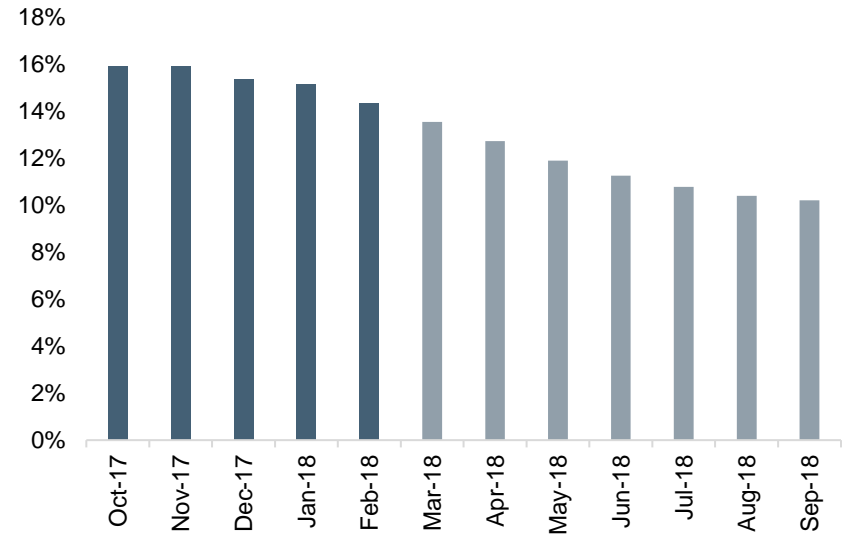
Figure 6: Avg. energy prices (N/litre) vs. Core & Transport Inflation (% YoY)



Source: NBS, ARM Research

Going forward, we expect the impact of high base effect to continue to dictate food inflation and overall headline trajectory. Also, ample market supplies and household stocks from the ongoing dry season harvest guides to stable MoM reading for food inflation and further deceleration in YoY food inflation although, we foresee mild price increases during the lean season – which occurs around the third quarter – due to limited market supplies. For the core basket, still elevated crude oil prices guides to higher PMS prices, but we maintain our stance that energy prices will be managed in 2018 and expect a stable rise in MoM core inflation. Also, we do not expect the proposed threefold increase in minimum wage to bring about a resurgence in inflationary pressures given that Nigeria’s inflation is largely cost push and not demand pull. Actual inflation numbers in January & February align with our bull case scenario at the start of the year hence, adopting our bull case forecast for inflation, we now expect March headline inflation to print at 13.6% YoY with mean headline inflation for 2018 forecasted at 11.7% YoY (2017: 16.6% YoY).

Figure 7: Inflation rate – Actual and Forecast (YoY)



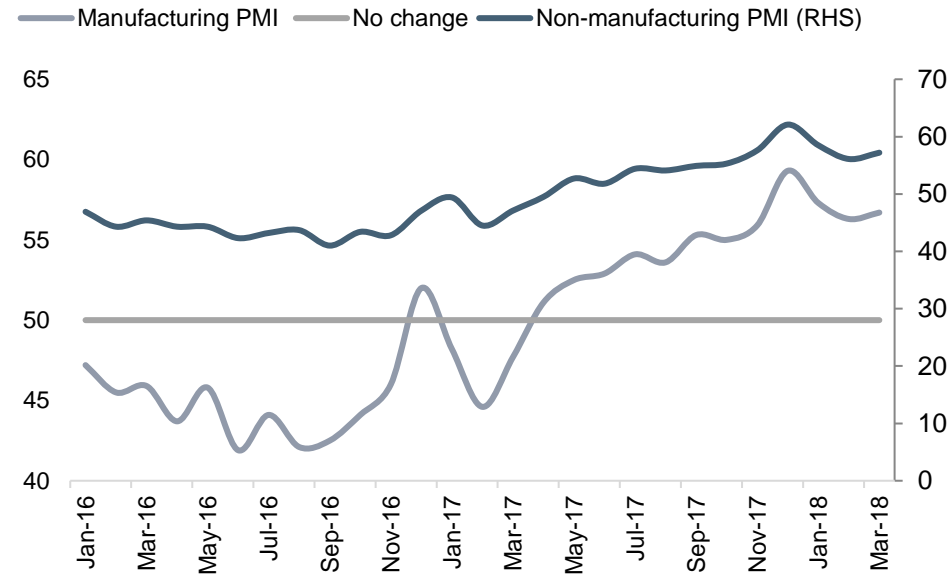
Source: NBS, ARM Research

March PMI: A cause for cheer

The CBN survey for the month of March revealed that business activity maintained its strong expansion, with the Manufacturing and Non-Manufacturing index printing at 56.7 and 57.2 (versus 56.3 and 56.1 in the month of February respectively). Much of the support for the Manufacturing PMI (Purchasing Managers Index) stemmed from a pick up in activities across the inventories, production level and new orders diffusion indices whilst the employment and suppliers deliveries expanded at a slower pace relative to the prior month. Elsewhere, the non-manufacturing PMI was buoyed by the expansion seen in the level of business activity and new orders whilst inventories and level of employment expanded at a slower pace. Across the subsectors, fourteen of the sixteen subsectors recorded growth in the period. For us, we perceive that the pick-up seen across these sub-indices reflects relative currency stability as well as increased lending to both households and corporates as revealed in the First Quarter 2018 Credit Condition Survey Report by CBN. Clearly revealed in the report is also the improved loan performance as measured by default rate. The foregoing combined with improved economic conditions has helped boost aggregate demand in the economy.

Though PMI remains a leading indicator of the level of economic activities, it is not a seamless guide for the level of economic growth in Nigeria. Nevertheless, improved oil receipts, currency stability and CBN support to agricultural sector is expected to support economy growth this year. Consequently, we forecast GDP growth of 3.1% for Q1 18 and 2.6% for FY 18.

Figure 8: Historical Movement in Purchasing Manger's Index



Source: CBN, ARM Research

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