

Macro Economic Report | Monthly Update

Macro Economic Update – May 2019

Improved liquidity, compelling case for near term stability

The liquidity in the Investor & Exporters Window (IEW) improved in the month of May, with inflows (Ex-CBN) accounting for 95% (April: 86%) of total outflow and the market closing with unmet demand of \$128 million (April: \$396 million). The lower unmet demand stemmed largely from faster decline in outflow (-14% MoM to \$2.5 billion) compared to 5% MoM decline in Inflow (Ex-CBN) to \$2.3 billion. Going by breakdown of inflow (Ex-CBN), the decline emanated largely from domestic participation at the window, with sales by non-bank financial institutions declining 32% MoM to \$496 million. On the other hand, offshore flows expanded by 7% MoM to \$1.7 billion, with FPI flows accounting for 90% of offshore funds. Notably, the increased FPI participation reflected in the fixed income market during the month, as average yields contracted 70bps to 12.94% (April: +5bps).

Reflecting the improved liquidity at the window, available data as at the time of writing showed absence of CBN sales, with the apex bank accruing a net purchase of \$396 million (April: \$768 million) to support the gross external reserve expansion by \$330 million (April: \$365 million) to \$45.5 billion. As a result, the naira was stable across markets, with the NAFEX and parallel rate closing the month at ₦360.74 and ₦359.39 against the dollar respectively.

While the elevated fixed income maturity level in the second half of the year heightens risk of repatriation, we believe the current ammunition at the behest of the apex bank and the call for dovish stance in advanced economies suggest little hurt to the reserve. As such, we maintain our expectation of near term naira stability.

Figure 1: Foreign Currency flows through the IEW (\$'bn)

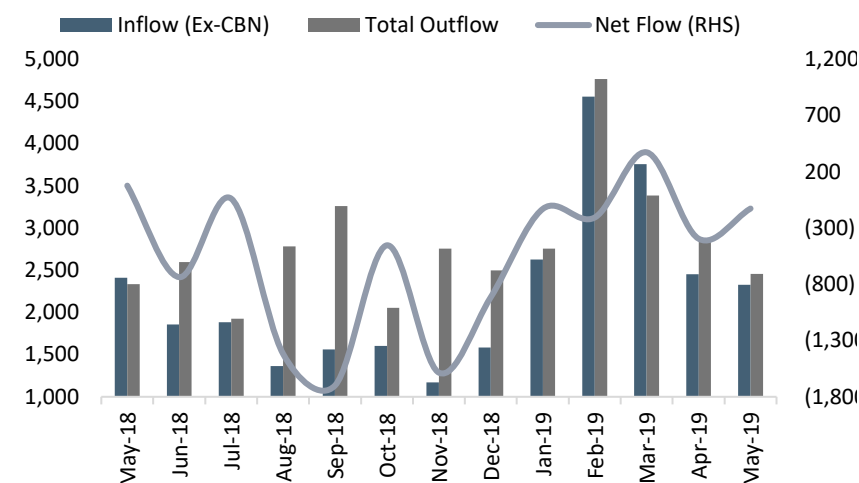
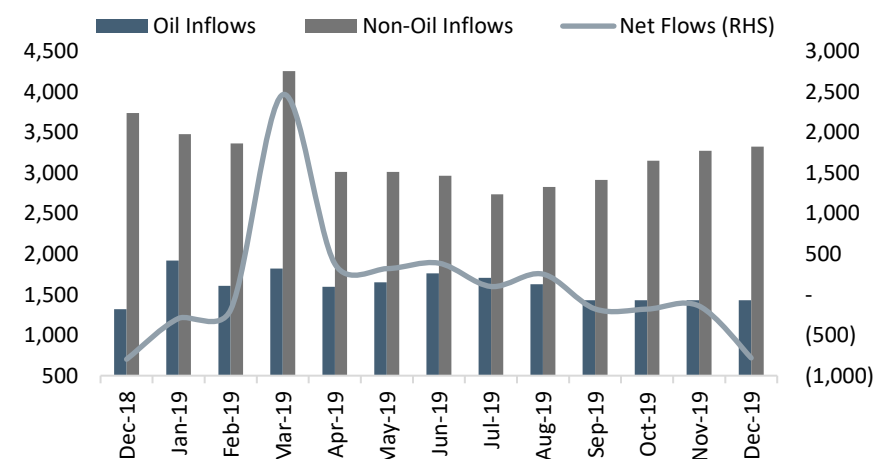


Figure 2: Foreign Currency flows through the CBN



Source: CBN, FMDQ, ARM Research

Inflation to move northward in May.

Inflation rate for the month of April took a different turn, printing at 11.37%, 12bps higher than numbers reported in the prior month. The outing mirrors a surprising uptick in food inflation, printing at 13.70% YoY (March: 13.45%) – overshadowing the moderation in core inflation to 9.28% YoY (March: 9.46%). On the food index, uptick in prices of farm produce which expanded by 47bps to 13.79% YoY led the increase. From data provided by NBS, the price increase was more evident in the Northwest and Eastern regions particularly Zamfara, Kebbi and Bauchi which is not far-fetched, given the emergence of clashes between security agencies and Armed bandits in these regions. Core inflation on the other end mirrors the impact of stable PMS prices at ₦145/litre, which outweighed increases in diesel (+12.9% YoY) and kerosene (+13.6% YoY) prices. Similarly, Month-on-Month inflation inched up by 16bps for the second consecutive month to 0.94%, mirroring increases in food and core inflation.

For the month of May, inflation rate is expected to tick up further to 11.39%, stemming from both the core and food indices. Starting off with the core index, we expect the impact of the increases in diesel (+12.9% YoY) and kerosene (+13.6%) YoY prices to be more evident this month, as declines in PMS prices (-3.6% YoY) gradually fades out. On food inflation, a directive to halt farming activities in Zamfara state was issued in the month of May in a bid to curb the conflict with armed bandit. The disruption to farming activities coupled with seasonal price increases (occasioned by Ramadan and lean season harvests) is expected leave inflation higher in May. Overall, our adjustment translates to an average inflation rate of 10.7% YoY over 2019 (FY 18: 12.2% YoY).

Figure 3: Avg. energy prices (₦/litre) vs. Core & Transport Inflation (% YoY)

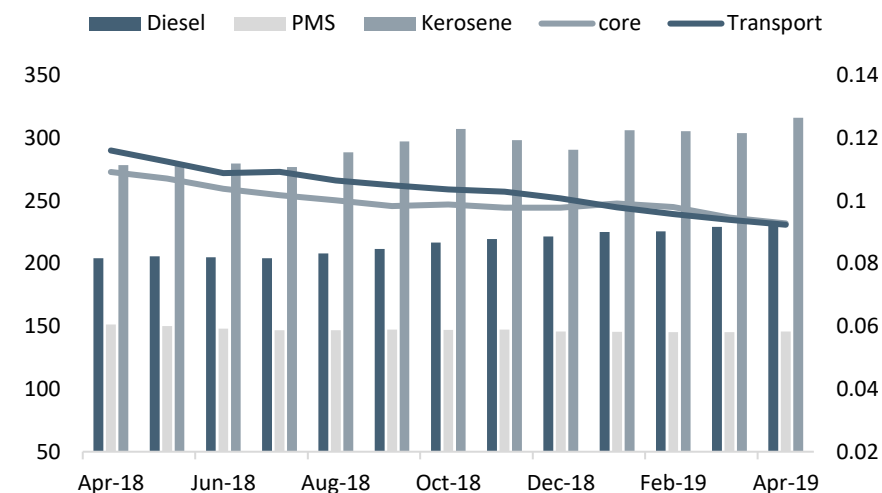
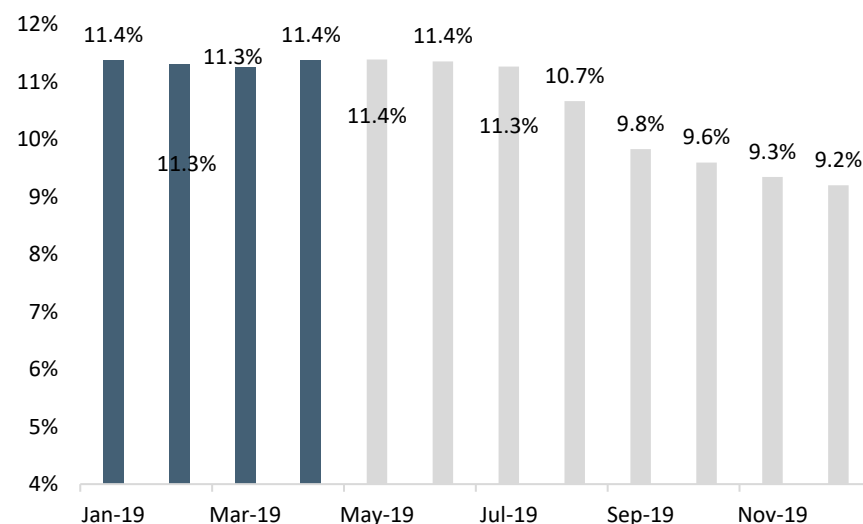


Figure 4: Inflation rate – Actual and Forecast (YoY)



Source: NBS, ARM Research

Q1 19 GDP: Strong start to the year but not great

The GDP numbers released for Q1 2019, showed the economy expanded by 2.0% YoY (Q1 18: 1.9% and Q4 18: 2.4%), as the resilient growth in the non-oil sector neutered contraction in the oil sector. On the former, the services and Agric sector (which accounts for majority of the economy led the momentum), with the sector growing by 2.5% YoY. On the flipside, oil sector contracted further by 2.4% YoY for the fourth consecutive quarter, mirroring the decline in crude oil production. Over the review period, average crude production printed at 1.96mbpd compared to a revised production level of 1.98mbpd in Q1 18.

Dissecting activities in the non-oil sector, notwithstanding conflict between the herders and farmers in north central and further escalation with armed bandit, which placed a drag on crop production, the Agricultural sector still grew 3.2% YoY as the presence of security forces slowed the pace of disruption. Also, the services sector grew by 3.1% YoY, mirroring an expansion in ICT (+9.5% YoY), Transport (19.5% YoY) and real estate (+0.9% YoY) amidst 7.6% YoY contraction in financial services. Clearly, improvement in ICT reveals increased subscriber base with voice calls expanding by 17.2% YoY and data by 14.2% YoY. Elsewhere, electoral activities in the first quarter slowed the manufacturing sector with companies within our coverage recording either a decline or slower growth in revenue over the period. Accordingly, the sector recorded growth of 0.8% YoY (Q4 18: 2.4% YoY; Q1 18: 3.4% YoY).

Over the rest of the year, we retain our expectation for most sectors with slight changes to the services and oil sector. On the former, with the substantial addition of 4.7 million subscribers between Q4 18 and Q1 19, we made an upward adjustment to our expectation of growth in the ICT subsector. That said, the services sector is expected to expand by 1.7% YoY in FY 19, albeit slower than the 3% YoY growth recorded over FY 18.

Figure 5: Historical movement in Oil, Non-oil and Real GDP

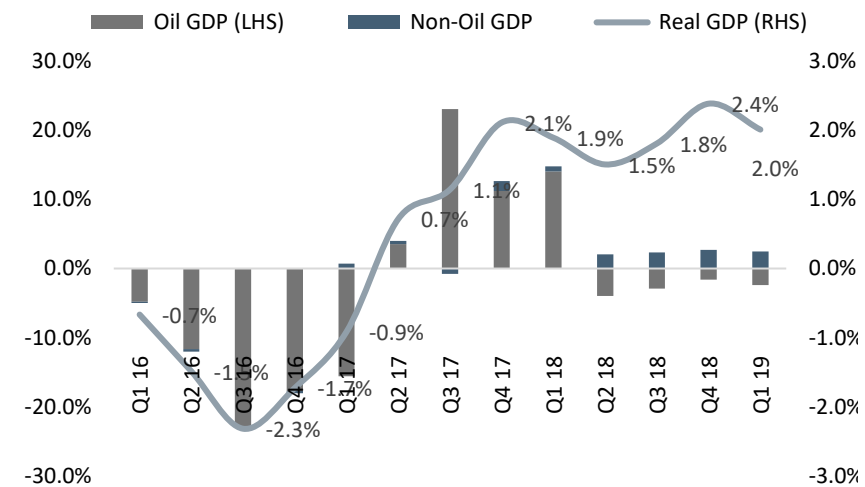
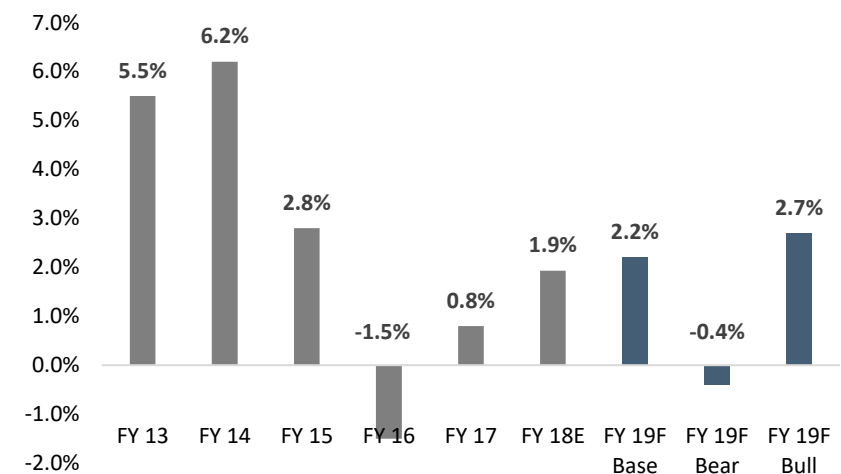


Figure 5: Historical movement in Oil, Non-oil and Real GDP



Source: NBS, ARM Research

Also for the oil sector, given the low base of oil production in the prior year and new oil production from Egina oil field which we expect to see more of its impact in the second half of 2019, we have revised our growth estimate to 6.1% (previously: 6.8% and FY 18: 1.1% YoY). The reduction in our growth forecast is based on the closure of Forcados and Nembe creek line due to pipeline leakages discovered in the second quarter of 2019.

For the Agric and manufacturing sectors, we believe the key catalysts are recent order from presidency to clear the Apapa gridlock and continued efforts of the government to curb the conflict situation in the north. However, we await progress from these initiatives before making revisions to our estimate. That said we expect the non-oil sector to expand by 1.8% YoY (2018: 2.1% YoY).

Table 1: YoY growth in key sectors and Real GDP

	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	FY 17	FY 18	FY 19E
Agriculture	3.4%	3.0%	3.1%	4.2%	3.0%	1.2%	1.9%	2.5%	3.2%	3.4%	2.1%	3.2%
Manufacturing	1.4%	0.6%	-2.9%	0.1%	3.4%	0.7%	1.9%	2.4%	0.8%	-0.2%	2.1%	2.1%
Services	1.0%	-0.5%	-3.1%	-0.8%	0.5%	4.1%	3.4%	3.8%	3.1%	-0.8%	3.0%	1.7%
Construction	0.1%	0.1%	-0.5%	4.1%	-1.5%	7.7%	0.5%	2.0%	3.2%	1.0%	2.2%	2.5%
Trade	-3.1%	-1.6%	-1.7%	2.1%	-2.6%	-2.1%	1.0%	1.0%	0.8%	-1.1%	-0.7%	-0.4%
Oil GDP	-15.6%	3.5%	23.0%	11.2%	14.0%	-4.0%	-2.9%	-1.6%	-2.4%	5.5%	1.1%	6.1%
Non-Oil GDP	0.7%	0.4%	-0.8%	1.5%	0.8%	2.0%	2.3%	2.7%	2.5%	0.5%	2.1%	1.7%
Real GDP	-0.9%	0.7%	1.1%	2.1%	1.9%	1.5%	1.8%	2.4%	2.0%	0.8%	1.9%	2.2%

Source: NBS, ARM Research

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