



Economic Research

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Economic Report | Monthly update

Economic Update – March 2013

Economic Snapshot

February 2014 Inflation Data/Indices

	MoM	YoY	Prev YoY
Headline	0.5%	7.7%	8.0%
Food	0.6%	9.2%	9.3%
All Items Less Farm	0.5%	7.2%	6.6%
Imported food	0.5%	7.2%	7.0%
Energy	-0.3%	3.7%	3.4%

Currency Markets

	Latest	Daily Chg	YTD
USDNGN	163.85	-0.03%	-2.21%
EURNGN	226.03	-0.38%	-2.61%
GBPNGN	274.37	-0.82%	-3.41%
JPYNGN	160.91	-1.24%	-5.71%

Monetary Aggregates – February 2014

	(N'bn)	MoM	YoY
M2	15,319	5.7%	-1.5%
CPS	16,668	1.8%	10.5%
NCG	-1,498	18.4%	-34.2%
NFA	7,557	-8.3%	-22.5%
NDC	15,170	0.4%	18.4%

External Position

	Latest	QoQ	YoY
Trade Balance (\$'bn)	9,035	-1.4%	1.4%
External Reserves (\$'mn)	37,972	-12.3%	-22%
Foreign Debt (\$'mn)	8,821.9	6.7%	35.2%

Growth Data – Q4 2013

	(N'bn)	%of total	YoY
Real GDP	65,259	100%	7.4%
Agriculture	14,033	21.50%	1.6%
Oil	8,941	13.70%	5.2%
Services	23,546	36.08%	9.5%
Wholesale and Trade	11,134	17.06%	7.8%
Manufacturing	5,163	7.91%	14.6%

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Inflation tracks lower on food price declines

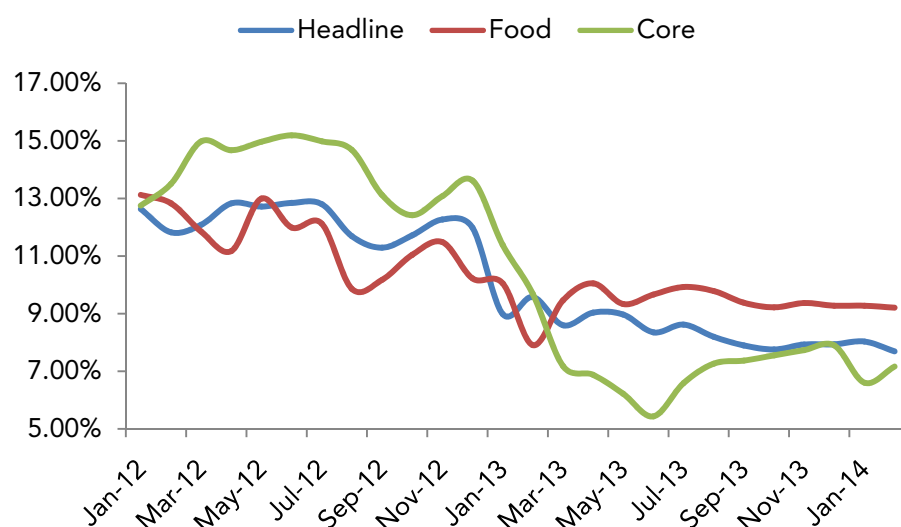
The National Bureau of Statistics (NBS) reports that YoY headline inflation declined to a 6-year low of 7.7% in February 2014 - 30bps lower than in January whilst MoM reading was 10bps lower than the preceding month at 0.5%. YoY core inflation resumed its uptrend after January's dip, rising 60bps to 7.2% with MoM reading also climbing 30bps to 0.5% over the month. The NBS linked the uptick in core inflation to observed increments in the costs of repairing household appliances and motor cars. Food inflation declined 10bps YoY and 20bps MoM to 9.2% and 0.6%, respectively with the NBS noting significant moderation in the prices of tubers, vegetables and meat. FEWSNET¹ notes that industrial and institutional purchases to replenish stocks which began later than normal—towards the end of February—left most domestic markets well supplied resulting in staple food prices being largely lower than February 2013 levels.

Going forward, core inflation is likely to rise quicker following several bouts of fuel shortages during March. Per food inflation, FEWSNET reports marked increases in area under cultivation across some northern states in February which it links to Federal Ministry of Agriculture and Rural Development (FMARD) dry season farming initiatives which will likely result in average to above average harvests for the dry season. This development, amidst further FMARD progress on storage following the completion of 20 new storage silos

¹ FEWSNET – Famine Early Warning Systems Network

in 2013—which brings total national capacity to 1.3million MT—and continued improvement in input distribution, broadens scope for an extension of the benign trends in inflation over 2014. Our forecasts for March inflation, which incorporate the possibility of a near term uptrend in food inflation—on the back of uptick in demand from large agro-allied firms—and continued rises in core inflation, is for a 20bps MoM increment to 7.9% +/- 20bps.

Figure 1: Trends in headline, food and core inflation



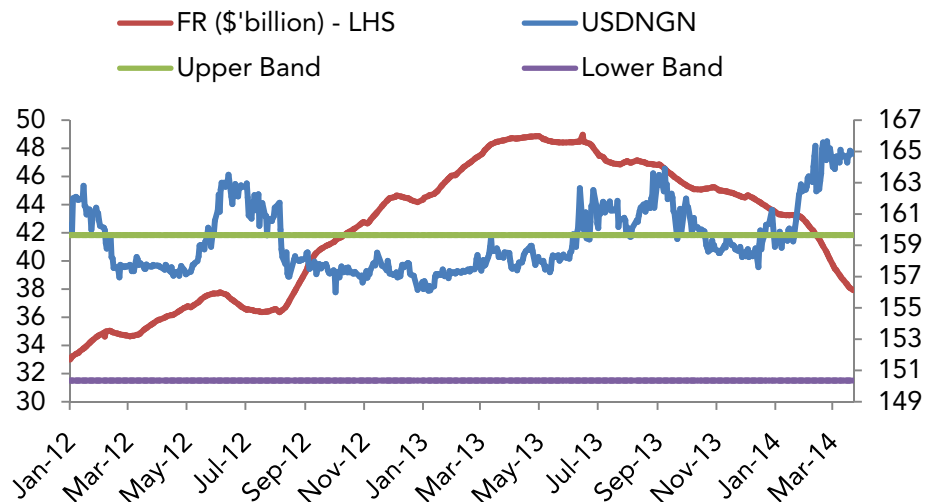
Source: NBS, ARM Research

Reserve accretion to slacken amidst new shocks to oil production

The USDNGN recorded a 0.1% MoM gain to ₦165.05/\$—its first positive month in 2014—mirroring a broad trend of gains across EM currencies in March. These improvements came despite the US Federal Reserve shaving a further \$10billion off its monthly large scale asset purchase (LSAP) program to \$55billion and lend credence to our earlier thesis about foreign portfolio investments (FPI) reversal front-loading the impact of Fed tapering during the bout of EM weakness in early Q1 14. Notwithstanding the MoM gain, heightened demand pressure persisted in March with monthly RDAS sales rising 14% MoM to \$3.5billion—a 7-year high. Consequently, foreign reserves declined 5.7% MoM to \$37.8billion (Feb: -7% MoM), which together with the

higher dollar sales suggests reserve inflows have improved. The latter possibility appears to underpin the MPC's reticence to adjust the Naira's trading band despite additional pressures from most recent FPI data which indicates a 43% MoM contraction in capital flows to \$683million.

Figure 2: Exchange rate and foreign reserves



Source: Bloomberg, ARM Research

However, reserve inflows are likely to weaken following the announcement by Shell in late March of a *force majeure* on the 400kbpd Forcados pipeline (18% of total production capacity). This should result in moderation to oil exports which together with flagging FPI inflows and sustained demand pressures continue to underpin our tame naira outlook over the rest of 2014.

Yields descend as MPC tightening falls short of expectations

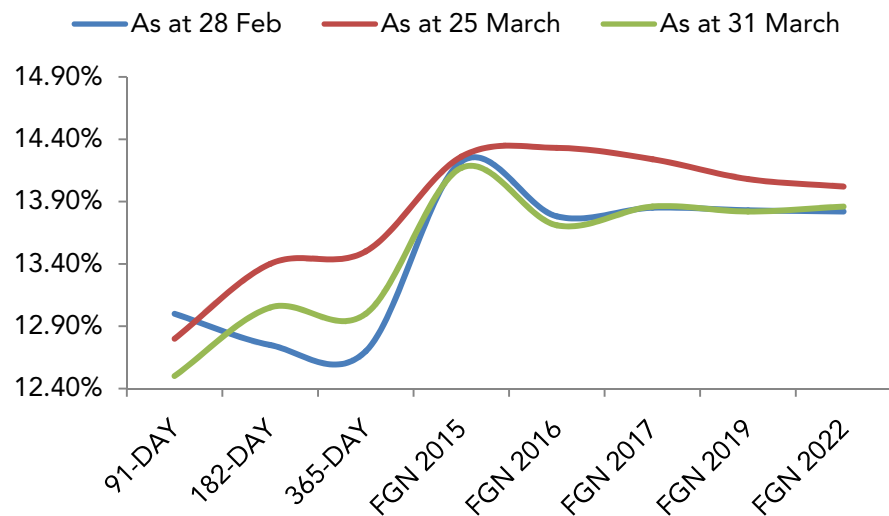
Although bill issuance (₦1.2trillion) rose by more than one-half MoM in response to maturing paper, net bill issuance remained negative for the fourth consecutive month (₦8billion²). Yield movement in March reflected a combination of the tighter liquidity conditions and expectations about monetary policy. The former factor weighed on yield direction in early March

² January (₦232billion) February (₦610billion)

as NDIC³ debits amidst delayed FAAC inflows drove an average 63bps increment in T-bill rates from the end of February and resulted in a spike in NIBOR rates to year highs (average: 18%). Rates remained at these levels through the March MPC, sustained by expectations of further public sector CRR hikes.

However, the decision by the MPC to only raise CRR on private deposits which amounts to a much smaller cull ~~~N~~300 billion (vs. ~~~N~~1trillion⁴ had public sector CRR been raised to 100%), saw markets heave a sigh of relief with T-bill yields declining 40bps on average post MPC levels to close March at 12.5%, 13.05% and 13% for the 91-day, 182-day and 364-day paper respectively. MoM, yields across the 182-day and 364-day remained 30bps higher, whilst the 91-day paper was 50bps lower as the curve normalized from February's month end inversion. A similar scenario occurred in the bond market where yields closed March flat MoM at 13.86%, 13.82% and 13.86% for the FGN 2017, 2019 and 2022 bonds respectively.

Figure 3: Yield Curve



Source: FMDQ, ARM Research

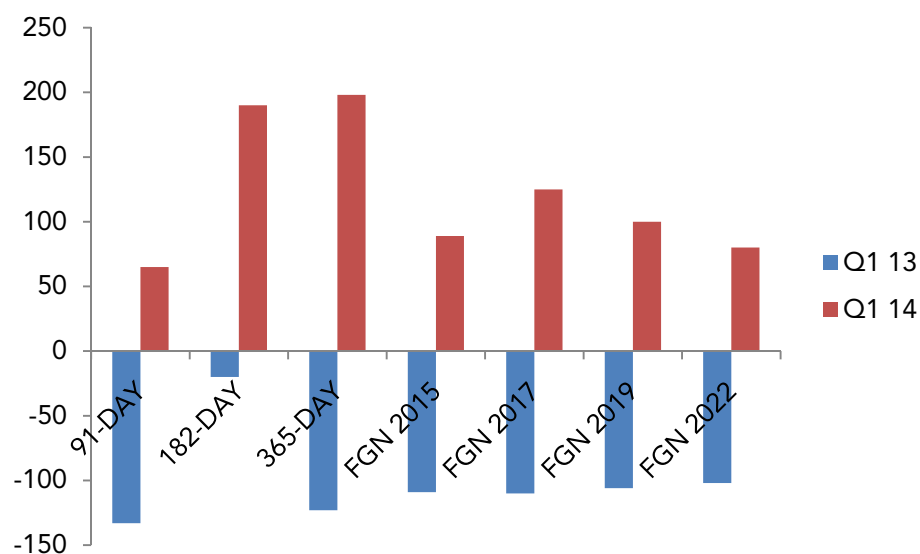
³ Nigeria Deposit Insurance Corporation

⁴ Using CBN data as at December 2013

In sum, the trend along the naira curve broadly fits into our views about sustained domestic appetite for securities acting to cap uptick in yields amidst a trend of declining paper supply. The latter trend continued in March with the DMO displaying rate sensitivity by issuing ~~₦85~~ billion vs. its proposed ~~₦90~~ billion with bid-cover ratios at 2.2x vs. 2.1x at the previous auction⁵.

In the near term, at least until June when the new governor resumes, we expect no major twists to monetary policy which will leave liquidity conditions as the key driver of yield movements. Farther out, the voting pattern at the MPC which displayed increased openness towards a rate hike by CBN members suggests this possibility is on the cards as other policy tools appear to be nearing their limits.

Figure 4: QTD Yield changes (bps)



Source: FMDQ, ARM Research

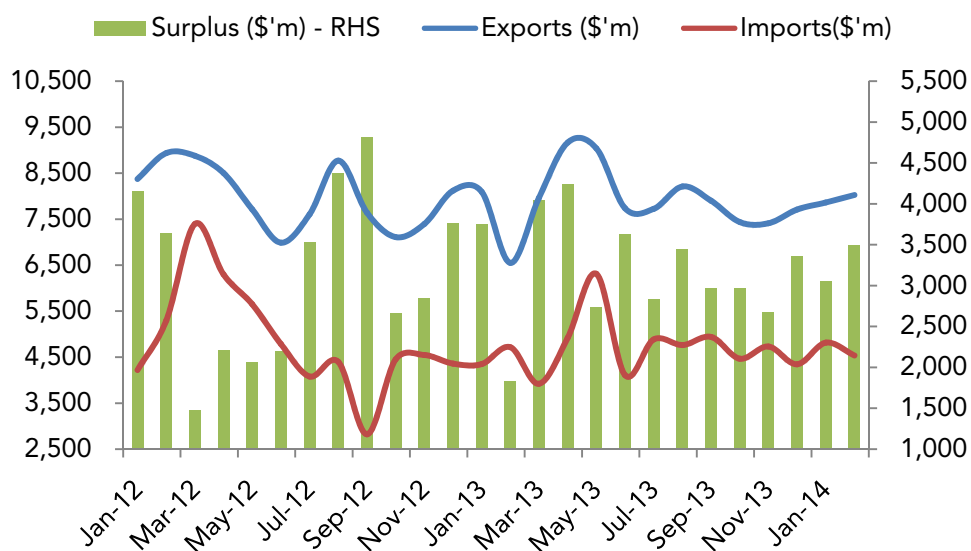
Trade surplus to weaken on softer oil revenues

Brent crude oil prices contracted 0.8% MoM to \$107.76/b on account of renewed concerns over Chinese GDP growth after weaker than expected export and industrial production data in March. The decline emerged despite

⁵ Total Q1 bond issuance is 30% lower YoY at ~~₦265~~ billion.

fresh geo-political risks arising from Libya, where unrest continues, and from the impact of sanctions on the world's third largest oil producer—Russia—after its military incursion into Ukraine. On the heels of the shutdown of the 95kbpd Nembe Creek Trunk line in late February, further pressures on oil exports emerged with Shell closing the 400kbpd Forcados pipeline in March. The size of the latter disruption relative to overall total production suggests more pressures for oil exports. Although oil imports are likely to have declined on account of the 13.3% QoQ decline in total PMS import allocations granted by the PPPRA⁶ to 26million barrels for Q1 14, the impact on overall imports is likely to be have been offset by the decision to put off the implementation for the new automotive tariffs till June 2013.

Figure 5: Monthly trade statistics



Source: CBN, ARM Research

In the near term, outlook for oil prices hinges on talks between P5+1⁷ countries and Iran (the second largest OPEC exporter) in April to monitor progress on January sanctions deal. Further progress amidst reports of a deal to re-open some part of Libya's oil fields could create a bearish trajectory for oil prices. This, together with the fresh production worries, is likely to drive a soft trend in

⁶ Petroleum Product Pricing Regulatory Agency

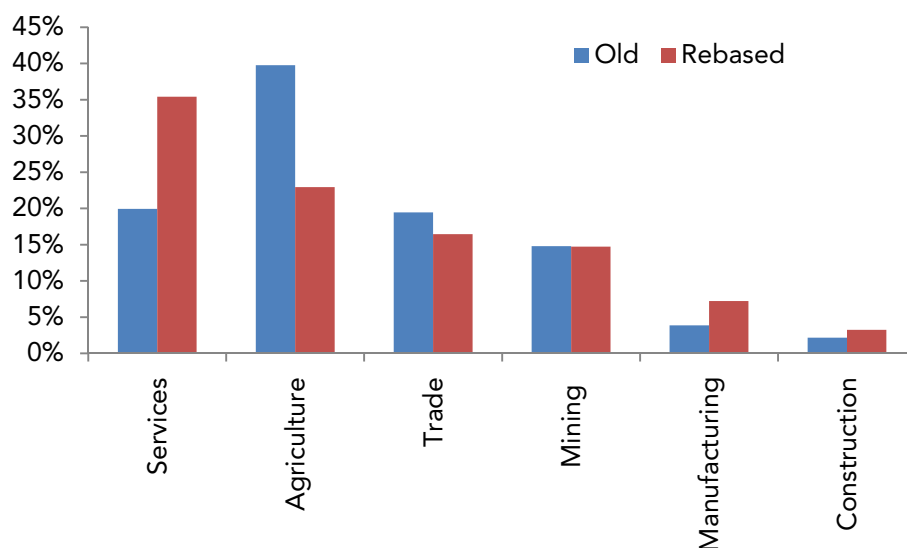
⁷ P5+1 countries are the five permanent UN security council members (US,UK, China, France and Russia) and Germany

oil exports. Vehicle imports are likely to trend higher ahead of the new June kick-off tariff implementation date, creating scope for an uptick in imports (~18% of total imports in the five years to 2012). Overall the weakness in oil revenues and an uptick in imports increase scope for a softer trend in the trade surplus.

GDP rebasing estimates reveals SSA's biggest economy

After several postponements, the NBS released the long-awaited preliminary estimates of the rebasing/re-benchmarking exercise with the nominal GDP for the new base year (2010) rising 59%—1ppt shy of the upper band of our forecast range— from previous to ₦54.2trillion (\$361billion). At ₦80trillion (\$510billion), forecast 2013 nominal GDP by the NBS, with the implied YoY growth at 7.4%, results in Nigeria becoming Africa's largest economy.

Figure 6: GDP: Sectoral Composition⁸



Source: NBS, ARM Research

In contrast to the paradox that existed under the old series where nominal and real GDP pointed to different sectors, the rebased series both confirm Services⁹

⁸ Data refers to average between 2010 and 2012.

⁹ Services, as defined here, excludes Wholesale and Retail Trade which the NBS release included.

position as the largest component of real GDP at ~36% vs. 20% under the old series. This sizable expansion in Services, which we anticipated on account of the various reform initiatives across Telecommunications, finance and real estate over the past decade, resulted in the sector accounting for ~three-quarters (45pps) of the 59% rebase ‘jump’. The core of these gains came from ICT which now accounts for 31% of Services GDP (vs. 7% in the old series) and includes the telecommunications, broadcasting and the new additions: publishing and motion picture. Other components of the rebased Services include real estate (22%), public administration (11%) professional and scientific services (9%) and finance (7%) amongst others.

Wholesale and Retail Trade, for its part, contributed the second largest to the rebase effect (13pps) which we believe reflects the relatively rapid formalization of growth in retail trade infrastructure and logistics that occurred within the period. Manufacturing contributed 9pps to the nominal GDP rebase increment with the gains reflecting larger weights for Food, Beverage and Tobacco—previously unreported—Cement, Oil Refining and Textiles. However, manufacturing share of overall GDP which expanded 5pps to 7% remains small relative to economies of similar size reflecting the still deficient state of electricity production and transport infrastructure—and potential for further transformation/growth when these enablers improve. As we anticipated, agriculture’s sizable weight in the old series muted scope for sizable gains with the former growth ‘powerhouse’ accounting for just over a tenth of the overall rebase ‘jump’.

In line with recent trends of a declining contribution, crude oil share of nominal GDP contracted 23pps to 16% post-rebasing. This reflects the impact of stalled progress on the PIB which has discouraged IOC interest in OML auction rounds since 2008. The resulting underinvestment in production and reserves expansion, amidst rising oil theft and illegal bunkering, largely accounts for the negative contribution (-18pps) of the sector to the rebase jump, according to our attribution analysis.

Overall the rebasing exercise which was notably supported by the IMF, World

Bank and AfDB reveal an economy that is effectively non-oil driven given the sizable investments inflows into other sectors of the economy on account of the various liberalisation reforms that occurred since 1999. In the immediate aftermath of the release, economic metrics provide a mixed picture with lower fiscal deficit and debt ratios likely to provide greater impetus for the FGN to implement its plan to reduce debt service costs by increasing foreign borrowings. However, the rebased numbers also reveal some underlying weakness with fiscal revenues as proportion of GDP (in particular non-oil taxes) which are now much smaller relative to EM peers and will likely result in a greater drive by the government to capture the large informal sector of the economy. Similarly, the rebased GDP reveals a smaller market capitalization to GDP ratio which should result in renewed efforts by the NSE to drive greater listings of unrepresented sectors of the economy. Overall, the clarity obtained by the exercise should drive some policy adjustments from Nigeria's economic and financial policy makers in the coming days.

Table 1: Selected economic metrics post rebasing (% of GDP)

	2010	2011	2012	2013
Current Account	3.7%	2.1%	4.5%	4.1%
Debt	9.7%	10.1%	10.7%	10.9%
Fiscal deficit	2.0%	2.7%	1.4%	1.6%
Non-oil Revenues	3.4%	3.6%	3.8%	3.4%
Market Capitalization	14.6%	10.3%	12.6%	16.5%

Source: NBS, DMO, FMF, CBN, ARM Research

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