



Economic Research

ARM Research

[research@armsecurities.com.ng](mailto:research@armsecurities.com.ng)

+234 1 270 1652

5 June 2015

## Economic Report | Monthly update

### Economic Update – May 2015

#### Economic Snapshot

##### April 2015 Inflation Data/Indices

	MoM	YoY	Prev YoY
Headline	0.77%	8.7%	8.5%
Food	0.93%	9.5%	9.4%
All Items Less Farm	0.60%	7.7%	7.4%
Imported food	0.86%	9.2%	8.8%
Energy	0.57%	7.5%	7.3%

##### Currency Markets

	Latest	Daily Chg	YTD
USDNGN	190.00	-0.05%	-8.48%
EURNGN	222.94	0.26%	-0.76%
GBPNGN	302.99	0.85%	-6.60%
JPYNGN	159.51	-0.13%	-4.62%

##### Monetary Aggregates – April 2015

	(N'bn)	MoM	YoY
M2	16,546	-1.6%	8.0%
CPS	18,639	2.5%	11.8%
NCG	-914	1.6%	-39.0%
NFA	6,023	-6.4%	-20.3%
NDC	17,724	2.6%	16.8%

##### External Position

	Latest	QoQ	YoY
Trade Balance (N'bn)	1,585	71.6%	-34.6%
External Reserves (\$'mn)	29,350	-4.6%	-20.3%
Foreign Debt (\$'mn)	9,711	2.02%	10.1%

##### Growth Data – Q1 2015

	(N'bn)	%of total	YoY
Real GDP	16,050	100%	3.96%
Agriculture	3,177	19.79%	4.70%
Oil	1,677	10.45%	-8.10%
Services	5,905	36.79%	7.30%
Wholesale and Trade	2,852	17.77%	6.47%
Manufacturing	1,716	10.69%	-1.75%

Philip Anegebe

[philip.anegebe@arm.com.ng](mailto:philip.anegebe@arm.com.ng)

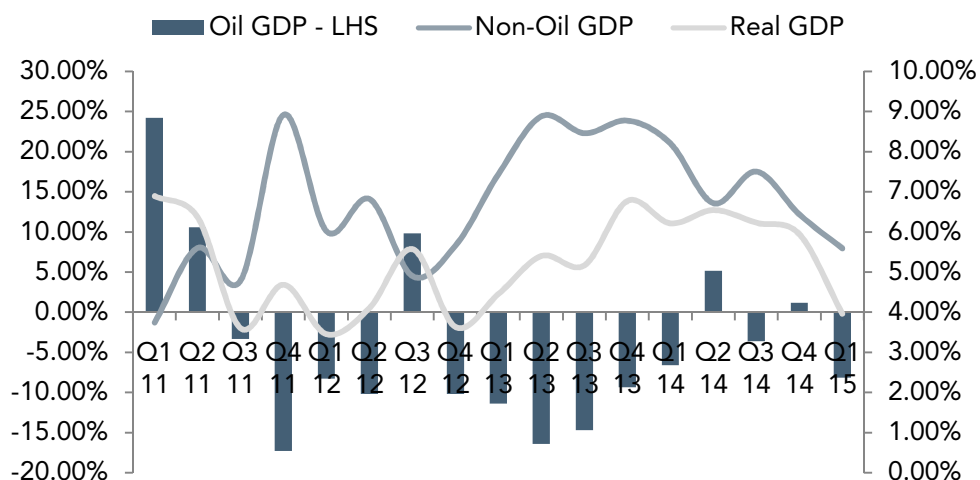
#### *Slump in rig counts and manufacturing slow GDP growth*

The National Bureau of Statistics (NBS) reported real GDP growth of 3.96% YoY in Q1 15--198bps and 225bps lower than in Q4 14 and Q1 14 respectively. Disaggregating the components, YoY non-oil GDP growth eased to its slowest in six quarters at 5.6%--260bps lower than recorded growth in corresponding quarter of 2014 and 80bps softer than in Q4 14, whilst oil GDP growth reversed the expansion of Q4 14, falling 5.1% YoY in Q1 15. The contraction in oil GDP was largely driven by supply-side constraints. More importantly, and according to OPEC, among member countries, Nigeria recorded the second sharpest drop in rig counts in March with production of 1.69mbpd in the month (vs. 2.21mbpd in the corresponding month of 2014). The slump in exploration, development, and production activities was tied to rising insecurity in producing areas (i.e. oil theft and pipeline sabotage) and, more importantly, NNPC's funding cuts on JV projects (-40% YoY to \$8.1 billion for 2015) with the agency's key partners also forced to scale down on capital expenditure and production. Of particular note, NNPC's inability to meet cash call obligation to JV partners appears to have been exacerbated by the significant fall in oil revenue.

Returning to non-oil GDP, Q1 15 slowdown mainly mirrored contraction in manufacturing as well as decelerations in agriculture and services components (which jointly account for 63% of non-oil GDP). Manufacturing GDP fell 1.8% YoY whilst growth in agriculture and services slowed 80bps and 30bps YoY to 4.7% and

7.3% respectively, in the quarter. Contraction in the former—manufacturing—stemmed from 54% and 5% YoY declines in oil refining, and textile, apparel and footwear (TAF) segments. Importantly, we believe the decline in the TAF segment continues to reflect impact of cheap imports which discourage local production. For services GDP, growth slowdown in the quarter was driven by 12.5% YoY contraction in its public administration sub-component.

**Figure 1: Changes in Quarterly GDP**



Source: NBS, ARM Research

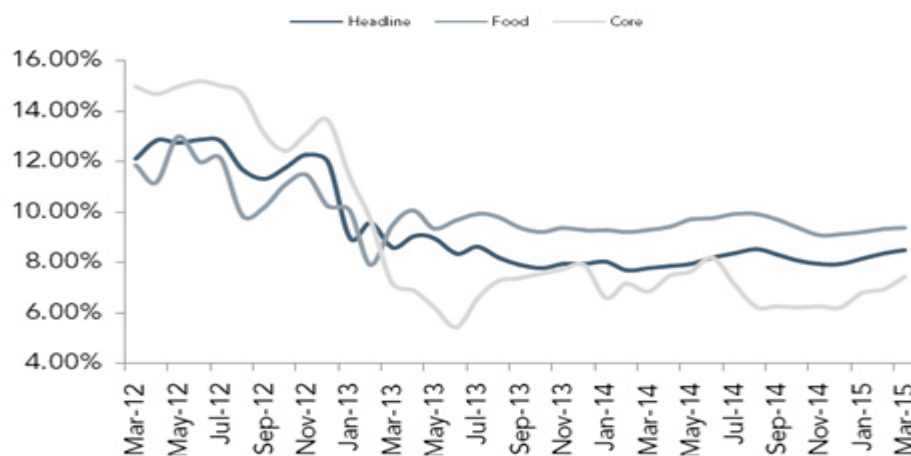
Going forward, with continuing local oil production sabotage and Nigeria's dwindling oil market share in Asia dampening hopes of a rebound in NNPC's JV funding, rig count in the oil sector looks set to continue its downward trajectory in the coming months. Furthermore, the growing cost of operation in the upstream sector underpinned by rising insecurity in the Niger Delta amplifies oil production concerns, raising scope for further contraction in Q2 15 oil GDP. Added to this, production downtime across companies in key sectors such as Telecomms, manufacturing, and banks following the recent fuel scarcity and oil marketers' strike action, amid pressures on discretionary income, is likely to drive further slowdown in non-oil GDP and ultimately contribute to slowing overall GDP growth in the coming quarter.

---

### ***Inflation accelerates to 23-month high***

The CPI for April 2015 rose 8.7% YoY (vs. 8.5% in March), in line with our estimate. Disaggregating the components, food inflation rose 11bps from March to 9.5% YoY largely underpinned by increase in processed food which jumped 97bps from March to 6.3% YoY in April, accounting for ~ 8.14bps of the 11bps rise in YoY food inflation. On the other hand, YoY farm produce reading was largely flat from prior month. The flatness in farm produce corroborates FEWSNET's report of low overall market demand in the period due to above average household food stocks following good main and off season harvest. Conversely, the jump in the former – processed food prices – is reflective of pass-through from currency depreciation as well as rising production cost on the heels of reportedly significant drop in power generation. On core inflation, which quickened 23bps from previous month to 7.7% YoY, NBS links price increases to sharp growth in price of clothing and footwear, furnishings and household equipment maintenance as well as restaurants and hotel divisions in the period.

**Figure 2: Trends in YoY headline, food, and core**



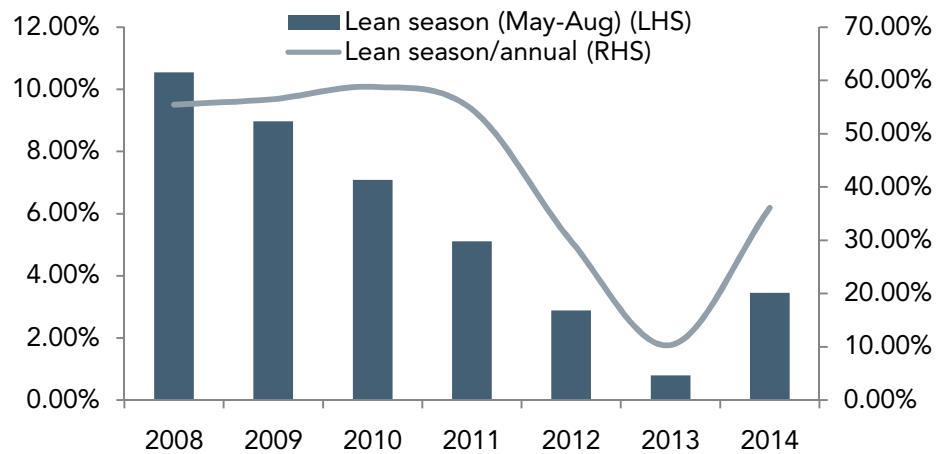
Source: NBS, ARM Research

### ***Rundown of food stock and fuel crisis to stoke further pressures***

As noted by FEWSNET, the moderating impact of carry-over stocks from

previous periods' harvest helped tame food inflation reading. However, as agricultural lean season approaches (i.e. May – August), we expect eventual depletion of household stock of foods to prop up market demand relative to shrinking supply, cascading to higher farm produce prices.<sup>1</sup>

**Figure 3: Average cumulative lean season inflation (MoM readings)**



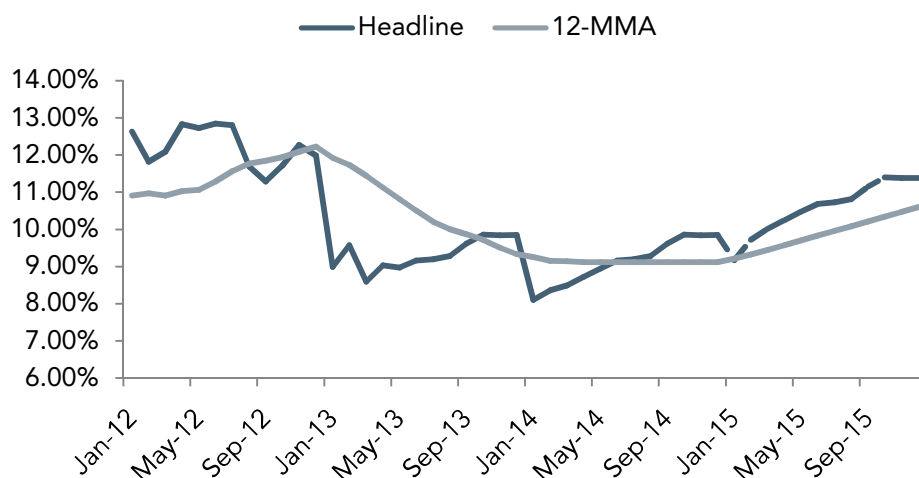
Source: NBS, ARM Research

On other fronts, recent passage of 2015 Appropriation Act which effectively excludes provision for fuel subsidy intensified ongoing arguments on complete deregulation and its expected effect on prices. In assessing the possible impact of subsidy removal, we take a cue from January 2012, wherein partial subsidy removal saw PMS price surge 50% to ₦97 and dovetailed to 210bps rise in YoY food prices to a then-fourteen month high of 13.1%. Incidentally, the recent crisis over subsidy payments and a new open-mindedness to the matter, on the part of both citizens and government, with several political figures having joined free-market advocates in calling for the abolition of subsidy suggest it may soon become reality. Thus, in the event of deregulation, as in 2012, we expect near term inflationary pressure: an ~164% jump in average PMS price to ₦230 in May 2015, with attendant effects on cost of transportation and food, has already set that cart rolling. In conjunction with the expected increase in food demand and commencement of the lean season, we forecast 30bps MoM rise in headline

<sup>1</sup> Relative to 2014 lean season, our more pessimistic stance for food prices is underscored by expected twin impact of lean season production pipe-low as well as the removal of fuel subsidy – a dimension that was absent in prior year – in the coming months.

inflation to 9% (+/- 20bps) in May 2015. Longer term, part and parcel of our anticipated subsidy-removal impact on inflation is a net deflationary effect as weaker consumer incomes reduce aggregate demand. Potentially, productive use of the subsidy savings (e.g. in infrastructure and power) could reinforce this dynamic by reducing supply-side bottlenecks which we have long believed are the underlying cause for elevated inflation.

**Figure 4: Inflation forecast**



Source: ARM Research

### ***Shock CBN tightening drives rise in yields***

The Central Bank of Nigeria (CBN) concluded its two day policy meeting on May 21, 2015, leaving Monetary Policy Rate (MPR) and its symmetric corridor at 13% and 200bps respectively by unanimous vote. However, following 9-2 vote in affirmative, the MPC harmonized public and private sector CRRs to a single 31% (vs. 75% and 20% for public and private previously), noting that the discriminatory CRR regime created room for moral hazards as well as constrained monetary policy efficacy. As noted in our previous communication on this topic,<sup>2</sup> juxtaposing the recent changes with the impact of the implementation of TSA in February 2015, which had been to drive a ~15pps MoM contraction in public sector deposit to 10% of the total ~N13 trillion banking sector deposit (2014 average: 22%), the CBN's new pronouncement

<sup>2</sup> "Initial thoughts post MPC: Tactical easing or tacit tightening?"

---

amounted to a net tightening with weighted average rate on total deposits now 31% (vs. 26% in April, 2015). In naira terms, our analysis indicates the CRR unification translates to net debit of ₦800 billion. Following the technical tightening, average FGN bond yield accelerated 240bps to 13.88% on 25th of May before eventually tapering off following eventual peaceful change of government, with yields closing May 2015 28bps lower MoM on average. Going forward, overlaying the CRR-driven withdrawals with OMO maturities of ₦217 billion in June (total bill maturities of ₦581 billion) should result in less liquidity in the system and a retracement of May's net decline in yields.

### ***Naira rises for third consecutive month***

The naira extended its gains for the third consecutive month, appreciating another 3bps to close May at ₦199.05/\$ even as forex reserves recorded a marginal rise (+28bps MoM to \$29.6 billion) for the first time in 2015. Similar to the case in preceding month, naira gains were largely supported by IOCs dollar sales in the period and the order-based 2WQ system that have left currency fairly stable since its introduction in February 2015 through, according to CBN, the stifling of speculative activities at the FX market. However, the 24% MoM jump in the size of foreign exchange transaction to ₦2trillion in April (vs. -50% MoM to ₦1.7 trillion in March) appears to have awakened the CBN to other drags on the currency. In particular, in response to the rise in dollar demand in April, CBN has had to step up its campaign against partial dollarization of the Nigerian economy with landlords and schools transacting local businesses in foreign currency receiving direct warning. Going forward, with the slight rebound in oil prices effectively reversed as at May and local crude production bedeviled by institutional and non-institutional constraints, both CBN and autonomous dollar supply are likely to be soft in the coming months, threatening recent exchange rate appreciation. Thus, pending when measures such as CBN's anti-dollarization campaign gathers momentum, there still remains significant scope for further currency pressures farther out.

---

Copyright © 2015 Asset & Resource Management Company Limited (“ARM”).

All rights reserved. Unauthorised use, reproduction, distribution or disclosure of this document is strictly prohibited.

This material has been issued by Asset & Resource Management Company Limited (“ARM”), a Company regulated by the Nigerian Securities and Exchange Commission. The analyst(s) primarily responsible for preparing this research report, in whole or in part, certifies that with respect to each security or issuer covered; all of the views expressed accurately reflect his/her personal views about the subject securities and issuers and no part of his/her compensation was, is, or will be, directly or indirectly, related to the inclusion of specific recommendations or views in the report.

This research report is based on information from sources that ARM and its analysts believe to be reliable. Neither ARM nor any of its research analysts, nor any member of the ARM Group, gives any representation or warranty, express or implied, or undertaking of any kind or assumes responsibility or liability of any kind with respect to the accuracy or completeness of the information set out in this report or any third party’s use (or the results of such use) of such information. This report is provided solely for informational purposes and is not to be construed as providing advice, recommendations, or endorsements of any kind whatsoever. The investments and strategies discussed here may not be suitable for all investors; counsel of investment advisor should be obtained with regard to such investments and or strategies. This research report is not a replacement for advice from an accountant, lawyer, personal finance advisor or other category of investment advisor. The investments discussed in this report may oscillate in price or value. Opinions and information provided are made as of the date of the report issue and are subject to change without notice. This research report is not intended as an offer or solicitation for the purchase or sale of any financial instrument. Reference herein to any specific security or financial instrument does not necessarily constitute or imply its endorsement or recommendation by ARM, its directors, officers, employees or designated agents. Members of ARM may act as broker, advisor or lender, or make a market in any investments or issuers referenced in this report. Further information on any of the securities discussed herein may be obtained upon request to ARM. By accepting this document, you agree to be bound by the foregoing limitations.