

Economic Report | Monthly Update

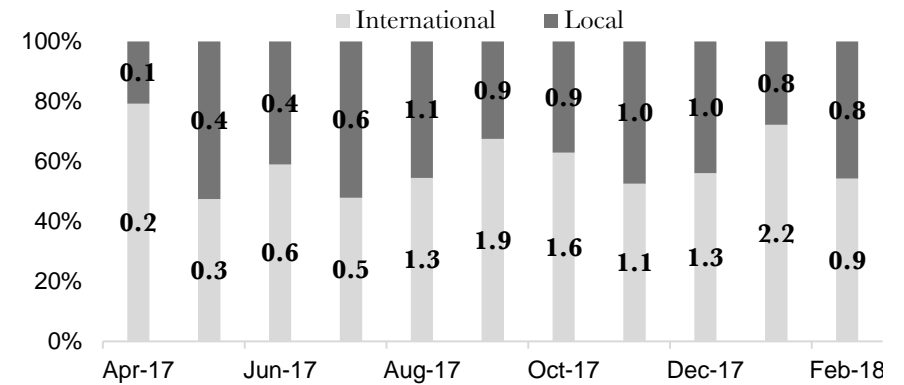
Economic Update – February 2018

Portfolio flows show signs of slowing

Although the Investor and Exporter Window (IEW) remained well lubricated with net-supply over the month of February at \$134 million, the figure came in lower than January print of \$274 million. Much of the decline emanated from a 26% drop in aggregate sales even as a 23% decline in aggregate purchases helped moderate the drop in overall net-supply. Parsing through the details, international inflows at the IEW dipped by 44% MoM to \$1.2 billion (\$2.2 billion in January) reflecting lower FPI (-45% to \$1.1 billion) as well as FDI (-26% to \$6 thousand). Elsewhere, CBN supply further dipped by 19% MoM to \$183 million (January: \$226 million), with the impact on domestic inflow (+28% MoM to \$1.0 billion) neutered by significant inflows from Exporters and Other corporates (+68% and +40% to \$115 million and \$754 million respectively). Consequently, overall supply printed at \$1.9 billion (January: \$2.6 billion).

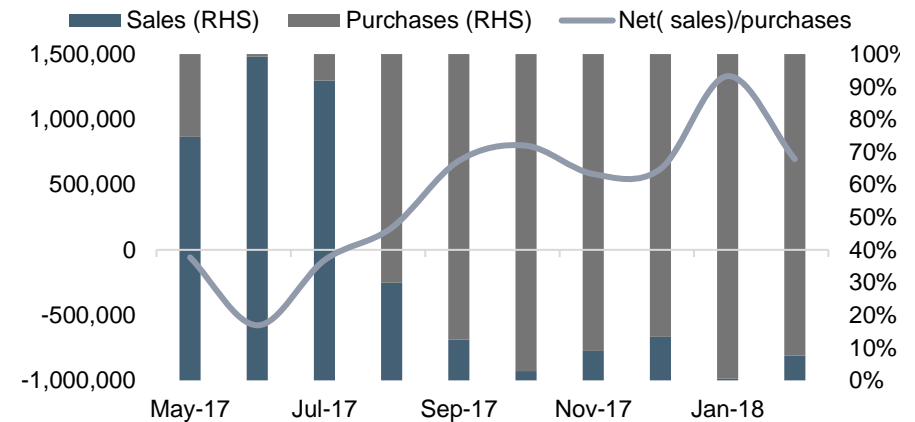
In terms of demand, \$1.7 billion was purchased over the review period, 23% lower than prior month's demand of \$2.3 billion. The lower purchase largely stemmed from a cutback in CBN purchases at the window. Since the inception of the window, the CBN had consistently mopped up the excess supply to shore up its reserve (up 4% MoM to \$42.49 billion) and maintain stability. For context, since September 2017, the apex bank accounted for average of 43% of total purchases at the window (with ~\$784 million average net purchase). In February, the CBN net purchase declined to \$695 million (\$1.3 billion in January), to account for 42% of the overall purchases at the window.

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)

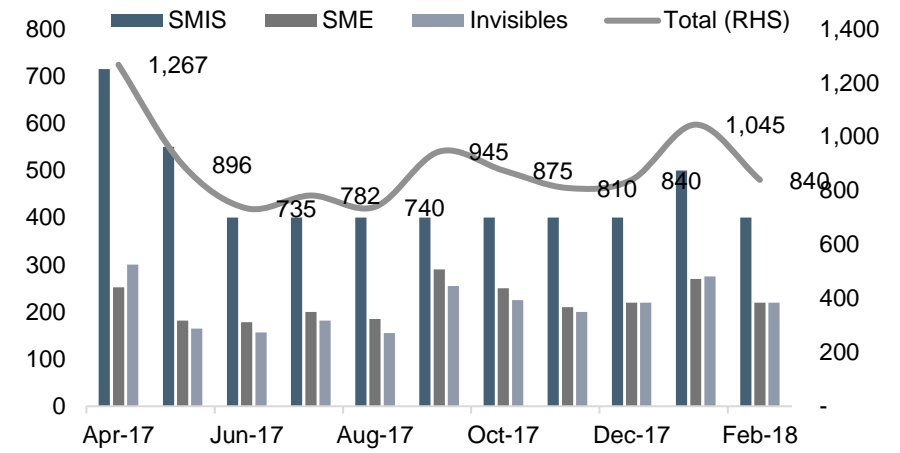


Source: FMDQ, ARM Research *Data estimated using monthly avg. exchange rate at the IEW*

Accordingly, daily average turnover dipped in February at the IEW (-28% MoM to \$198 million), with corresponding total transaction shedding 34% MoM to ~\$4.0 billion. Notwithstanding the tepid flows, the naira continued to show relative stability at the IEW as well as the parallel market. At the latter, the naira extended gains, albeit moderately to close at ₦361/\$ (+0.24% MoM) as the apex bank sustained sales across segments of the market while the NAFEX rates was relatively flat, closing at ₦360.19/\$ which is lower by -0.04% MoM. To further limit the overall cost of sourcing FX for invisible transactions, the CBN abolished all related commission charges on retail foreign exchange transactions, which had hitherto raised the cost of sourcing a dollar for invisible transaction by ~₦1.

Given the sizeable FX reserves (compared to our estimate of \$40.6 billion for February), the apex bank would have ample ammunition to continue the aggressive dollar sales in the near term. Adjusting for the proceeds of the recently issued \$2.5 billion Eurobond, we estimate a reserve position of ~\$48 billion by end June 2018, and possibly crossing \$50 billion by end year. Also, factoring in outflows via maturing money market instruments by foreign investors (30% of total maturing bills estimated at \$9.5 billion) and maturing swap positions of \$2.5 billion, and netting off the accretion in the reserves in excess of \$14.5 billion – amidst monthly average flows from oil and non-oil of \$1.7 billion and \$2.6 billion respectively, we believe the reserves will end the year relatively upbeat, thus keeping the FX market stable.

Figure 3: CBN supply to different segments of the market



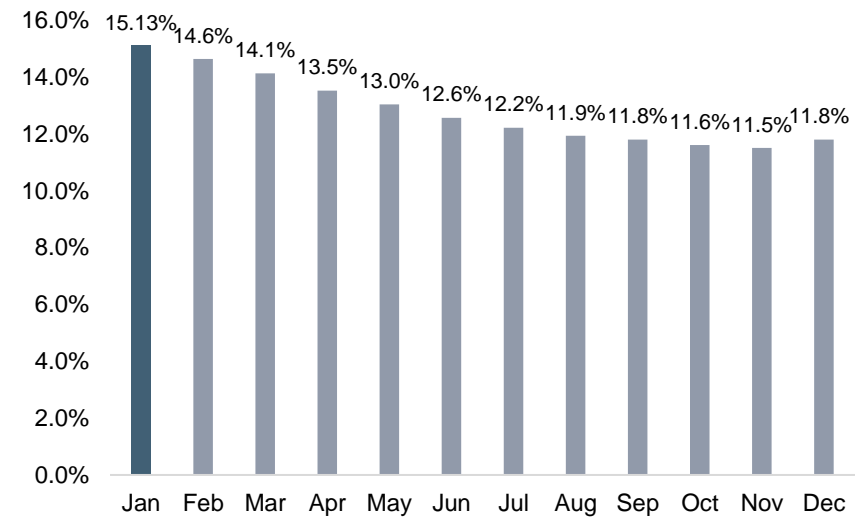
Source: FMDQ, ARM Research

Inflation: Base effects come into view

In line with our expectation, January headline inflation printed at 15.1% YoY, 24bps lower than prior month's inflation of 15.4%. The decline, reflected the impact of base effects in January 2017 from higher food prices following rising demand pressures from neighbouring West Africa countries looking to take advantage of currency-induced price competitiveness of Nigerian farm produce. However, looking at the monthly reading, we saw a resumption of cost pressures as MoM printed at 0.80% (+21 bps higher than 0.59% in the prior month) with pressures emanating from core (+17bps to 0.68% MoM) and food baskets (+29bps to 0.87% MoM). On the former, subsisting pressures were broadly evident across all subdivisions with the sharpest jumps emanating from processed food (+72bps), Restaurants (+16bps) and HWEGF(+15bps). The pressures on the HWEGF basket likely stemmed from rising energy prices (Kerosene: +1.7% MoM, Diesel: +3.9% MoM, PMS: +11.1% MoM) which also impacted on transport inflation (+6bps).

Over the near term, subsisting pressure on core inflation from higher crude oil as well as the negative consequences of higher energy prices on food inflation via passthrough from transport inflation remain key pressure points on MoM inflation. Furthermore, the pass-through of prices, given higher crude oil prices, would become difficult in 2018 as the election season picks up, thus hurting fuel supply. Consequently, expected series of scarcity as NNPC remains the sole importer, is expected to lead to higher selling prices across most states with expected pressure on transport. That said, we expect a continued downtrend in food inflation and overall headline trajectory on the back of high base effects from last year elevated food prices. Against this backdrop, we now look for headline reading of 14.6% YoY in February.

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

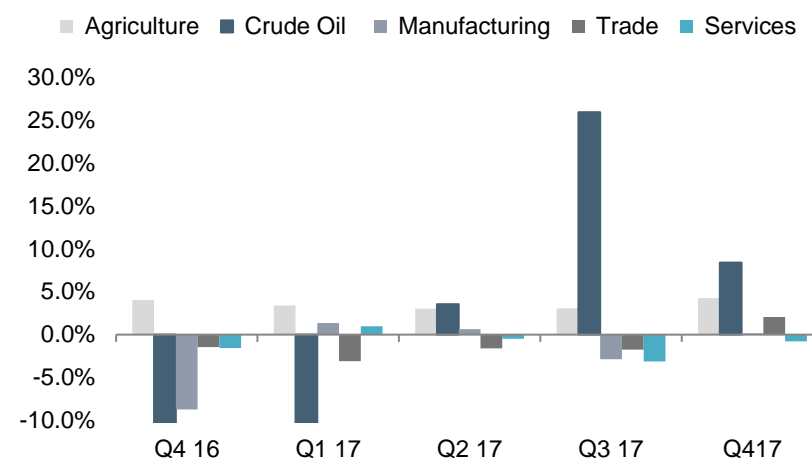


Source: NBS, ARM Research

Nigerian Economy grows 0.8% in 2017

The Nigerian economy accelerated its recovery story in the last quarter of the year printing at 1.9%. Much of the growth was buoyed the faster pace of growth in Agriculture¹, recovery in Trade, construction, and Manufacturing² sectors, as well as slower contraction in services³. Looking through the breakdown, accelerated growth in Agriculture was underpinned by favourable weather, increased cultivated land and sustained focus of the FG on the sector via various support programs. On manufacturing, although oil refining remained in negative territory (-46.2% YoY), faster growth in food, beverage & tobacco (+2.2% YoY) and Textile, Apparel & Footwear (+1.6% YoY) served as pillars in pushing the sector back to a growth of +0.1%. Elsewhere, slower contraction in services stemmed from ICT sector (-1.5% YoY) as mild growth in data output (+3% YoY to 95 million subscribers) was able to tame the impact of declining voice output (-7% YoY to 142 million active subscribers) on the industry's total output. Accordingly, non-oil sector grew by 1.5% in the review quarter. On the oil sector, relative to the double-digit growth (+25% YoY) reported in Q3 17, the pace of Oil growth slowed in Q4 17 (+8.4% YoY), reflecting a higher base in Q4 16 relative to Q3 16. According to NBS, oil production for the quarter averaged 1.9mbpd, +8.5% higher than 1.76mbpd. In summary, contrary to the oil-led growth in the last two quarters, support from other non-oil sectors (Ex – Agric) moderates concerns on the fragile nature of the economy recovery. Over laying the Q4 growth with the first three quarters takes the full year GDP to 0.8% (2017F: 0.6%).

Figure 5: YoY growth in Agric, Manufacturing, Services, Trade, Oil Sectors



Source: NBS, ARM Research

¹ Agriculture (Q4 17: +4.2%; Q3 17: 3.1%)

² Trade (Q4 17: +2.1%; Q3 17: -1.7%), Manufacturing (Q4 17: +0.1%; Q3 17: -2.9%), Construction (Q4 17: +4.1%; Q3 17: -0.5%)

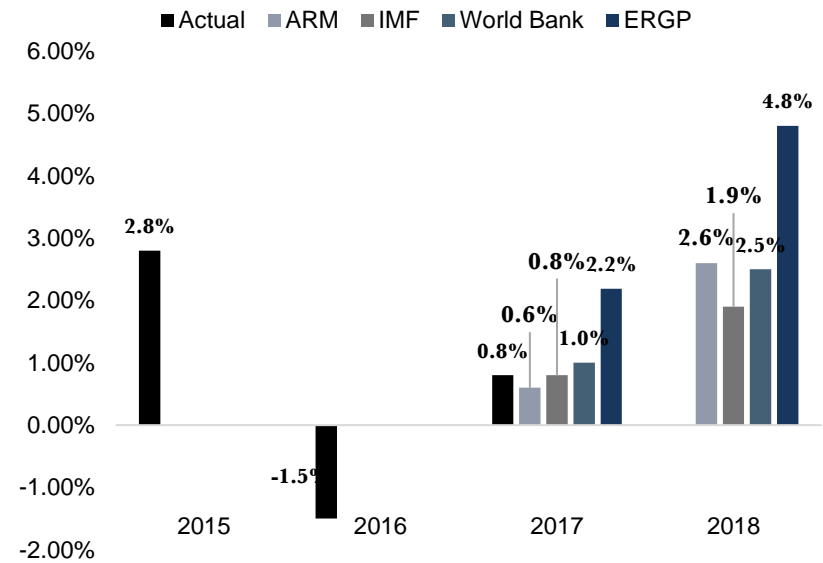
³ Services (Q4 17: -0.8%; Q3 17: -3.1%)

Recovery to grind on

Having factored the recent developments seen in the economy, we revise our growth estimate for FY 2018 to 2.6% (previous forecast: 1.9%). Starting off with the oil sector, we revise our oil production estimate to 2.1mbpd on the back of the Egina field project coming on board this year with capacity to add 200kbpd to crude output. This brings our oil sector growth estimate to 9.1% YoY (prior forecast of 8.3%). On the non-oil side, we increased support from the government on the agricultural sector bolstering output in the sector which drives our growth estimate of 3.3%. For context, in addition to cheaper loans and provision of fertilizers to farmers, the FG recently kicked off plans to address concerns around annual post-harvest losses estimated at 51.3 million MT. Elsewhere we expect the services sector to grow by 1.4% YoY with adjustments stemming from ICT and financial services. On ICT, though output from voice calls is still expected to decline slightly, efforts to boost data output would mask the decline in voice. In addition, election induced consumer spending and FX availability guides to a further improvement in the manufacturing which we estimate to grow +2% YoY. Particularly, recent moves by the apex bank to shore up its reserves moderates the likelihood of a shock to the currency in the coming months. Consequently, we forecast the non-oil sector will grow by of 2% YoY in 2018.

Over the first quarter of 2018, we expect the economy to grow by 3.1% YoY. Much of the support is expected to come from the low base of oil production in a similar period of 2017. Therefore, relative to Q1 17, we expect oil sector to grow by 19.1% YoY. On the Non-Oil side, we expect growth from the agricultural, services and trade sectors to support the non-oil sector and forecast a growth of 1.6% YoY.

Figure 6: YoY growth in Agric, Manufacturing, Services, Trade, Oil Sectors



Source: NBS, ARM Research

Ratings, Disclosure & Disclaimer – [Click here](#)