

7 February 2020

Macro Economic Report | Monthly Update

Macro Economic Update – January 2020

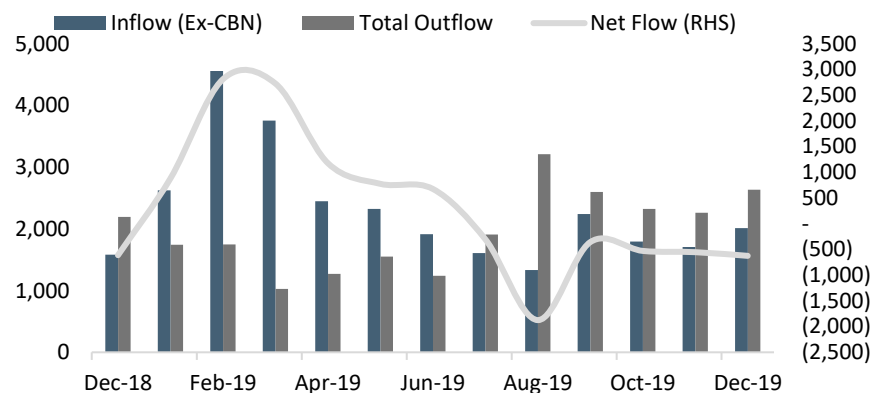
New year, new flows!

Movement of FX flows at the IEW took a different turn over the first month of the year. To buttress, after six consecutive months of net outflow at the window, balance of flows printed at a net inflow of \$561 million in January 2020. Interestingly, the net inflow was driven by a combination of higher inflows (ex CBN) and a 19% MoM decline in outflows (\$2.1 billion). With total FI maturity during the month estimated at \$7.8 billion (with foreign holdings of \$2.6 billion), we believe the lower outflows reflected lower repatriation of funds. On inflows, while local inflows (ex CBN) declined by 57% MoM, offshore inflows took the center stage, expanding by 178% MoM to \$2.2 billion – the highest in 10 months.

Reflective of increased offshore inflows, the CBN for the first time in seven months became a net buyer, net purchasing to the tune of \$248 million at the window. Elsewhere, CBN's intervention at other windows moderated slightly. However, the gross reserve was depleted to the tune of \$585 million to close at \$38.0 billion. Given the positive trend in flows at the IEW together with lower interventions at other segmnts, we think the decline in reserve could be link to a combination of lower oil inflows, other official receipts and higher official payments.

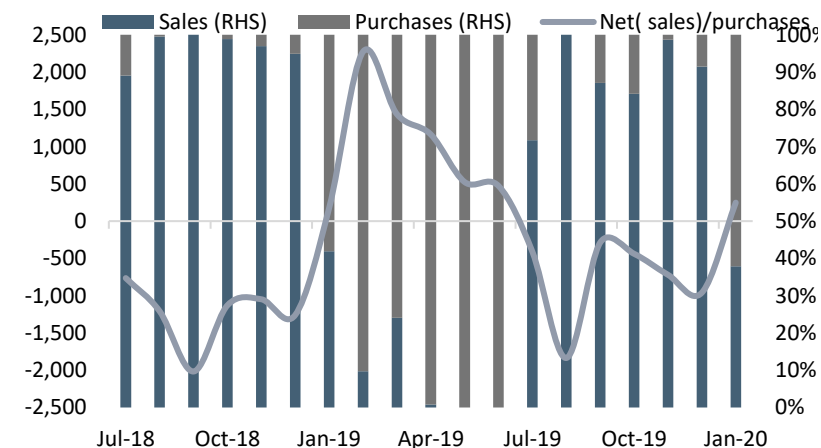
Going into coming months, while elevated OMO rates still offers an incentive to FPIs, we see more downside to inflows given FPIs concern on Nigeria's FX, particularly with oil price currently hovering at \$55/bbl. Irrespective, we still believe the CBN would continue to hold tightly unto the naira given reserve level expectations. Particularly, we see the FX reserve ending H1 2020 at \$34 billion and H2 2020 at \$31 billion.

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



Source: FMDQ, ARM Research

Figure 2: CBN activities at the IEW (\$'bn)



Source: FMDQ, ARM Research

Low base effect sends inflation on an upward trajectory – for now.

Inflation for the month of December printed at 11.98% YoY, 11bps shy of our estimate and 13bps higher than the prior month (November 19: 11.85% YoY). The uptick in inflation mirrored increases in food and core inflation by 18bps and 33bps to 14.67% and 9.32% respectively. Unsurprisingly, the impact of festivities as well as the lingering influence of border closure contributed to the hike in food inflation. Precisely, increase in food components such as processed food (+330bps) and imported food (+5bps) YoY outweighed moderation in farm produce (-10bps). Akin to food inflation, core inflation rose during the period hinged on uptick in core subcomponents including clothing (+12bps), furnishing (+6bps), health (+15bps), transport (+8bps), while HWEGF flatlined. On a MoM basis, headline inflation moderated 17bps to 0.85% MoM driven by a 28bps decline in food inflation to 0.97% MoM which reflects moderation in farm produce (-38bps to 0.91% MoM). Meanwhile, core inflation ticked 2bps higher to 0.81% MoM.

For the month of January, save the loitering impact of border closure on headline inflation, we do not see any pressure in food and core inflation. On the former, while main season harvest of major staple cereals such as maize, millet, rice and tubers has been concluded, market supplies remain buoyant, according to FEWSNET. This, in addition to the harvest of sorghum - a long cycle crop – guides to lower pressure on food prices. On core inflation, we expect less pressure hinged on stable energy prices and currency. Against this backdrop, we expect uptick in inflation by 11bps to 12.09% YoY in January and 1bps to 0.85% MoM, with average inflation rate for 2020 in expected to print at 13.0% (FY 19: 11.4%).

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

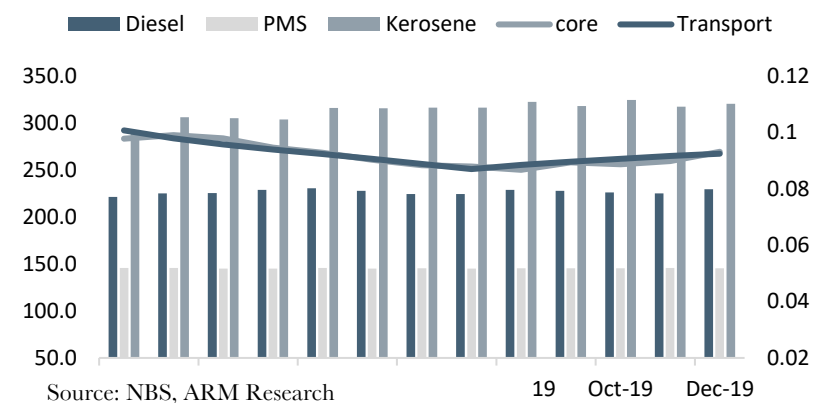
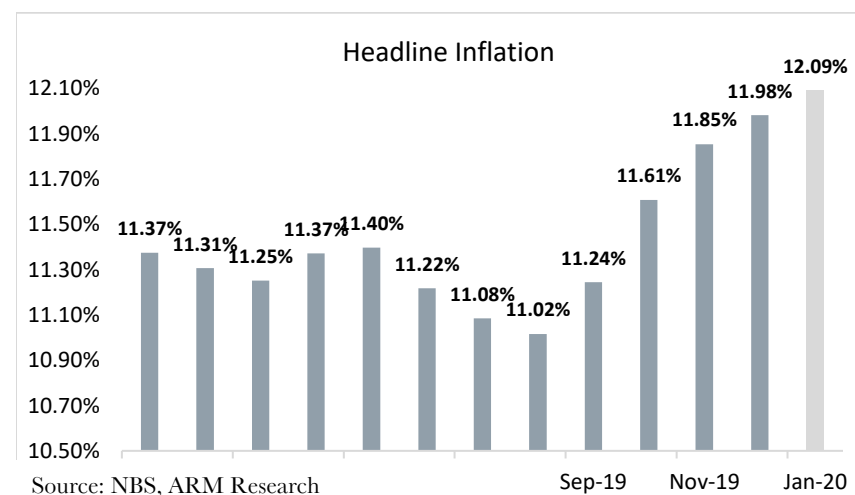


Figure 4: Inflation rate – Actual and Forecast (YoY)



Oil prices whipsaw in January

Oil market took on a volatile start to the year, with average oil price printing \$1.2 lower to \$64/bbl in January from \$65/bbl in the previous month. The month resumed off a bullish end to 2019, after OPEC and allies voted to increase oil production cuts by 500kbpd to 1.7mbpd while the demand picture got a boost from the part-resolution of the US-China trade rift after signing the phase 1 trade agreement.

Fresh bullish sentiments surfaced at the start of the month, following intensified tensions in the middle east. The disagreements between the US and key gulf producers, Iran and Iraq, sparked fears of war break outs. This posed a key threat to supply, particularly in OPEC's second largest producer, Iraq (4.6mbpd), which makes up 15% of the cartel's total supply (ex-condensates). This pushed prices to the month's peak of \$69. Meanwhile, we also noted the widening bonny-brent spread to \$2.51/bbl, the highest since July 2014. This came in line with our expectations, as the IMO 2020 regulations kicked off.

The bullish gyration was short-lived, as oil prices took a nose-dive to the month's trough of \$59 at the tail-end of the month. This was largely due to the outbreak of the Coronavirus in China which dimmed the positives serenading demand. The bearish sentiment was further exasperated by the builds in US crude stocks (YtD: +1.8mbpd vs 2018: -6.1mbpd), while production in the US touched a new record-high of 13mbpd.

Overall, we retain our 2020 average oil price forecast of \$61/bbl. which is hinged on our expectation of a higher net surplus of 0.45mbpd. This follows our forecast of increased supply from the US and other non-OPEC producers. The demand leg is also faced with fresh concerns on the Corona virus, which the WHO has declared an international emergency. Infact, there are talks of an emergency meeting by OPEC which has historically wound up in increasing production cuts.

Figure 4: Oil price movement (\$/bbl.)

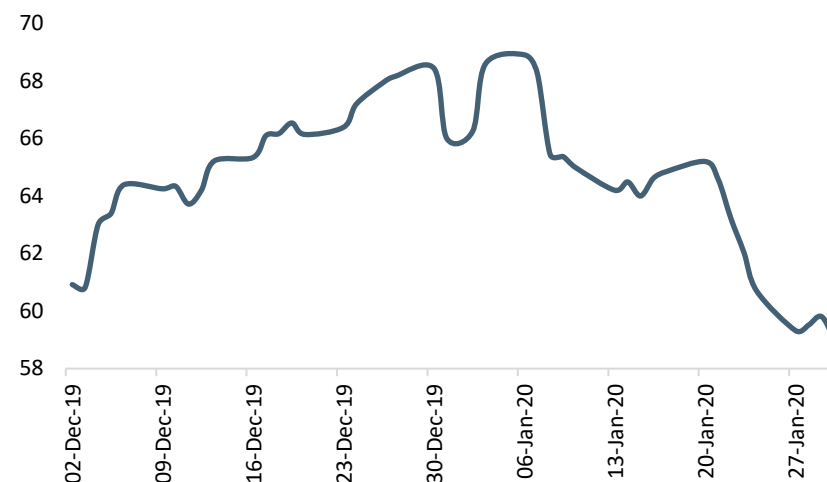
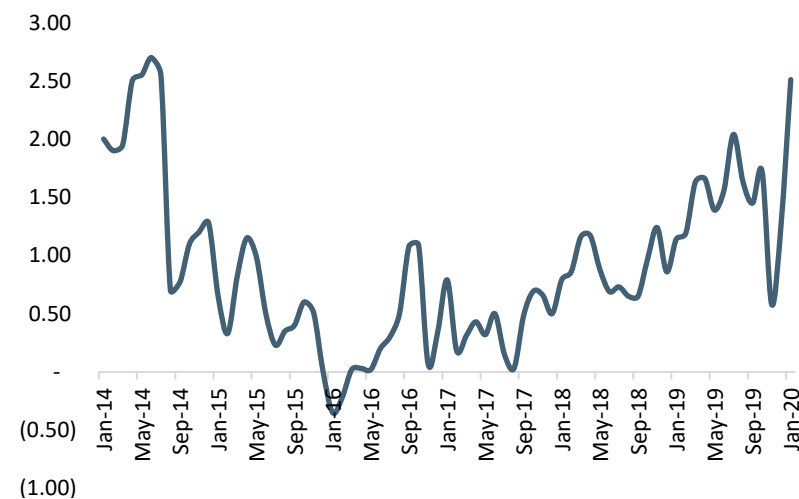


Figure 5: Bonny-brent spread (\$/bbl.)



Source: Bloomberg, ARM Research

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