

February 7, 2022



Nigeria Strategy Report

H1 2022

Domestic Economy and Policy Environment

Gross Domestic Product - Rebound in the Oil Sector and Resilience in the Non-Oil Sector to Boost Output

Executive Summary

The Nigerian economy sustained its recovery the second recession in a decade evidenced by positive performances in Q1 and Q2 2021, it continued the path in Q3 2021 GDP growth came in strong at 4.03%. Although Q3 growth slightly lags Q2 growth of 5.01%, we note that the rapid growth in Q2 and Q3 2021 were mainly supported by the base effect from 2020 when the economy contracted 6.10% and 3.62% in Q2 and Q3 2020 respectively. Overall, economic growth for the first nine months of the year printed at 3.17%, indicating paced recovery from the 2020 downturn (9M 2020: -2.69%).

Overall, economic growth for the first nine months of the year printed at 3.17%, indicating paced recovery from the 2020 downturn (9M 2020: -2.69%). Q3 2021 performance was predominantly a non-oil sector play as the oil sector contracted -10.73% - the sixth consecutive quarterly decline. On the flip side, the non-oil segment-maintained recovery, as the country fully reopened and economic activities resumed, with an impressive 5.44% YoY growth (Q3 2020: -13.89%).

In 2022, the IMF projects a 2.7% growth for the economy. The organization based its forecast on outperformance in the non-oil sector (especially services) and recovery in oil prices and this aligns with our base case (2.6%). We expect the oil sector to exit contraction with 1.7mbpd (incl. condensates production levels, slightly higher than 1.62mbpd recorded in 2021 hinged on the fixing of the Forcados terminal. Hence, we envisage a 5% growth in the oil sector in 2022. OPEC recently raised its production level and increased Nigeria's allowable production to 1.7mbpd and we expect a further increase in 2022, thus creating an incentive for FG to address the underproduction problem.

In this report, we focus on developments in the domestic environment, highlighting our views on the drivers for growth in 2022.

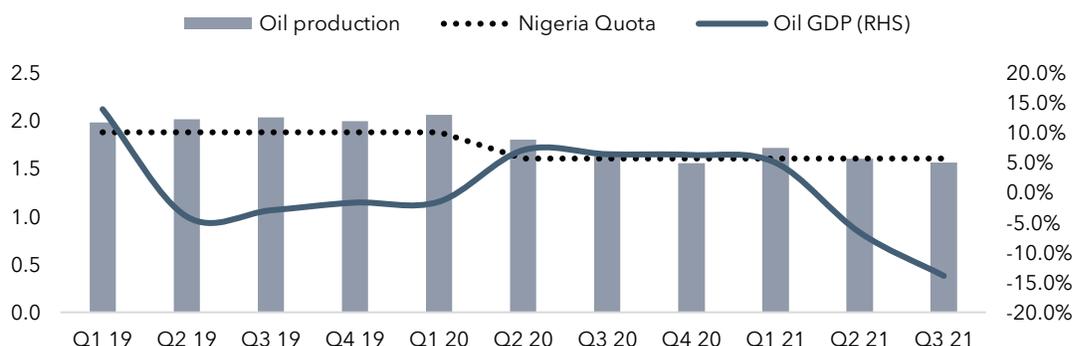
Q3 GDP... Services Sector Leads Sustained Recovery as Oil Sector Remain in Contraction

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Low Production levels kept Oil Sector in Contraction

Despite the ease in oil supply cuts by OPEC to a limit of 1.6mbpd at its August meeting, Nigeria’s oil volumes remain tepid at 1.27mbpd (excl. condensates), lower than 1.34mbpd in Q2 and OPEC-permitted production levels. Technical issues including pipeline weakness and leakages constrained oil production and stifled the growth in the oil sector. Hence, it recorded the sixth consecutive quarter of contraction (-10.73% growth YoY) in Q32021. Although Nigeria has consistently requested for a review of the baseline for OPEC’s Quota (which is currently set at 1.829mbpd) to allow for increased production in line with capacity, it has consistently met a brick wall due to current lower-than-quota oil production.

Figure 1: Trend in oil production vs Nigeria’s Quota and oil GDP



Source: NBS, ARM Research

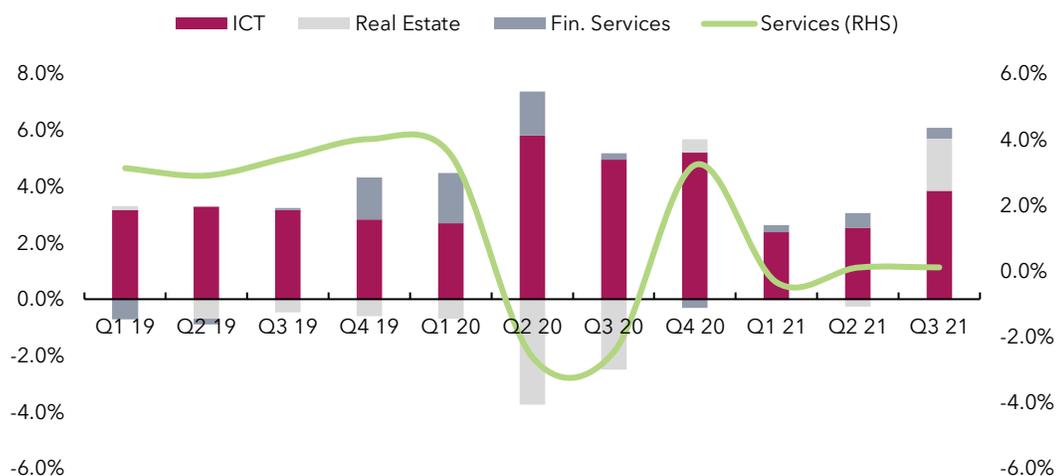
On the flip side, the non-oil sector rebounded with a 5.44% growth (Q32020: -2.51%) buoyed by improvement in services, manufacturing, and trade as growth in the agricultural sector slowed in the quarter.

Services Chaired Non-Oil Sector Growth

Services, which constitute the largest component of the non-oil sector, reported an impressive 7.0% YoY growth in Q3, the sharpest quarterly growth since Q1 2015. Telecommunication services chaired performance in this sector with a 10.9%. Although the pace of expansion has slowed from the pandemic-induced highs when digital services and virtual meetings became prominent, the sub-sector remains promising.

Financial services also posted a surprising 23.2% growth after two quarters of contraction with financial institutions reporting 25.5% expansion, as data from the CBN reveals increased credit to the private sector and financial results of some banks shows higher incomes from fees and commissions.

Figure 2: Attribution analysis of services GDP sector growth and key sub-components



Source: NBS, ARM Research

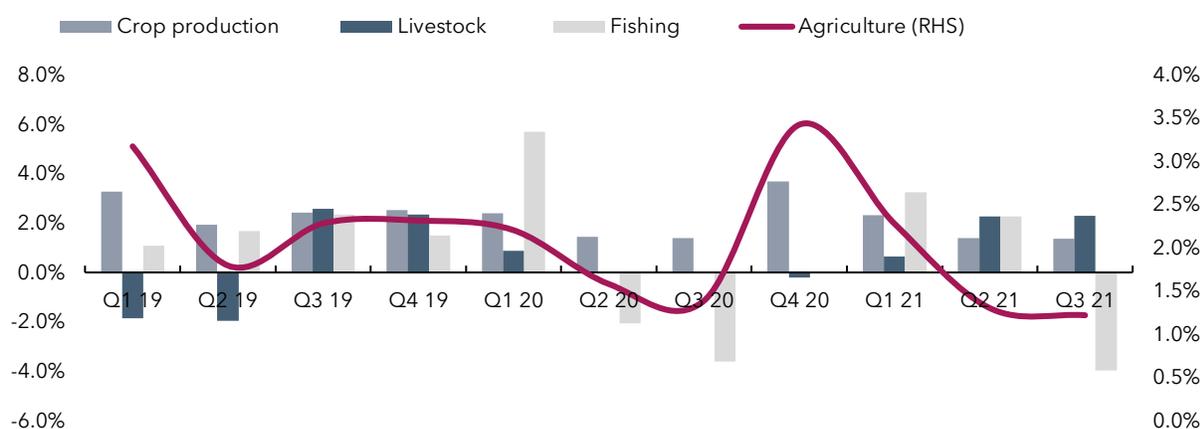
Manufacturing Sector Sustains Rebound

For the third consecutive quarter, the manufacturing sector posted positive performance (+4.3%), sustaining the rebound from the downturn in 2020. The sector continues to reap the benefits of improved economic activities as Nigeria sets sail in her quest for economic normalization.

Agriculture Sector Posts Weak Growth

The sector recorded its weakest growth since Q2 2018 (+1.2%), as it posted a 1.2% growth in Q3:2021 as it underperformed in the quarter. The sector had remained resilient even at the peak of the pandemic and expanded steadily. We suspect insecurity in the food-producing regions as the cause of the poor outing given that floods were minimal during the period. Crop production, the largest sub-sector, steadied at 1.4% growth as reported in Q2 while Fishing saw a 4.0% contraction. This trajectory defies the series of CBN’s intervention in the sector as the CBN governor alluded to a disbursement of ₦954.27bn between September and October 2021 to the sector under various initiatives at the November MPC meeting.

Figure 3: YoY Agric GDP growth vs Crop production, Livestock & Fishing



Source: NBS, ARM Research

Trade Sector Feasts on Base Effect and Land Borders Reopening

The trade sector fed off the reopening of the Nigerian land borders to recover from the nine-quarter contractions that pre-dated the pandemic, by recording expansion in Q2 and Q3. In Q3, the sector grew by 11.9% (Q2: 22.5%), however, it is also noteworthy that base effect and the improved demand for merchandize are partly responsible for the strong numbers as trade declined 16.6% and 12.1% in Q1 and Q2 2020 respectively.

For Q4 2021, we expect GDP to grow by 3.7% feasting on low base effect from the flattish growth from 2020. We expect the oil sector to remain in contraction as oil production in October and November averaged 1.38mbpd according to OPEC estimates, and below OPEC-allowed quota. We forecast a 2.6% FY growth for 2021 in line with IMF’s forecast for Nigeria. We expect oil sector to contract by 7.7% on the back of underwhelming production while the non-oil sector should grow by 3.7% YoY in 2021.

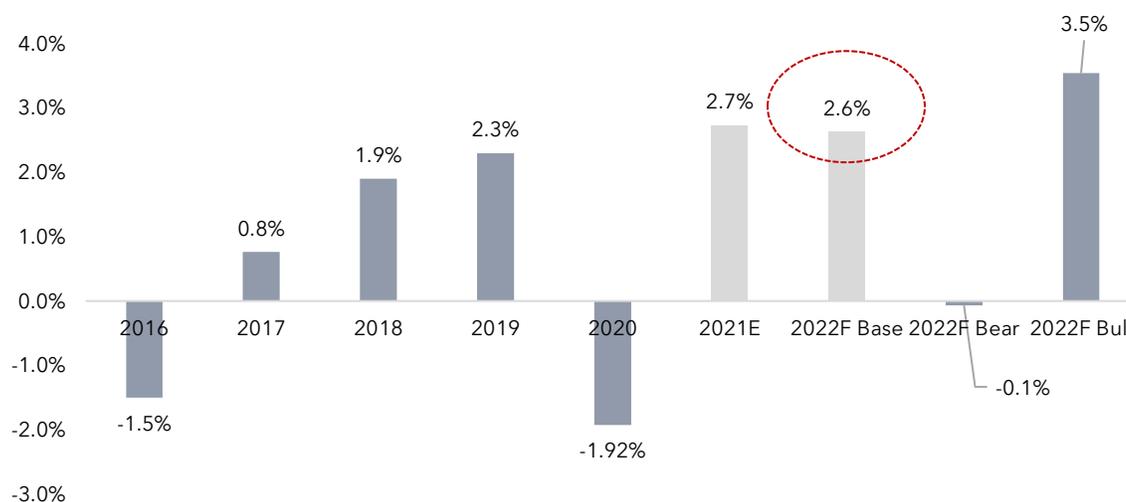
2022 GDP Outlook... Rebound in the Oil Sector and Resilience in the Non-Oil Sector to Boost Output

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The non-oil sector is expected to chart a new path in 2022, as the base effect from 2020 wanes off and output returns to pre-pandemic levels. We see sustained growth in the non-oil sector driven by resilience in agriculture and sustained positive performance in the services sector following the end of SIM cards registration and activation suspension and increased digitalization. For financial services, we are not optimistic of a sustained double-digit growth as banks’ interest income suffers from constant CRR debits. The construction sector may also enjoy pre-election rollout of funds for Capital Expenditure in 2022.

Major risks to our forecasts list as the defiant variants of the virus that could result in fresh lockdowns and distort expectations for oil demand and prices, FX illiquidity remains a major clog to strong growth in the manufacturing and trade sectors. However, given the recent updates emerging concerning how the Omicron virus portends the likelihood of an end to the protracted virus concerns since 2019, there is more room for optimism.

Figure 4: Annual real GDP growth and forecast



Source: NBS, ARM Research

Looking at the other scenarios, a bull case growth estimate of 3.5% is hinged on oil volumes matching OPEC's new quota at 1.7mbpd, solid growth in Agriculture, Manufacturing and Trade sectors as well as sustained momentum in the Services sector. These estimates also assume stable oil prices barring lockdowns and supply cuts from OPEC+ alliance. To the downside, renewed widespread lockdowns on the back of deadlier variants of the virus, oil price crash and poor production volumes should feed a -0.1% contraction in the bear case.

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