

# Nigeria Strategy Report

## H2 2019

### Domestic Economy and Policy Environment

## GDP: Modest growth, not much solace

### Executive Summary

The Nigerian economy expanded by 2.0% YoY for the first quarter of 2019 led by improved activities in the non-oil sector even as low crude production drove a contraction in oil sector. The services sector and Agric sector which accounts for majority of the economy led the momentum, driving an expansion in non-oil space by 2.5% YoY. Suffice to say, while the outturn in the Agriculture sector at 3.2% aligned with our surmise – activities in the services sector exceeded our expectation as an unanticipated level of improvement in voice subscribers left the output in the information and communications technology (ICT) sector stronger, with growth at 3.1%. On the flipside, oil sector contracted further by 2.4% YoY for the fourth consecutive quarter, mirroring a decline in crude oil production.

Central to our outlook over the rest of 2019 is the impact of recently discovered pipeline leakages, production activities at the Egina Oilfield, recovery in both the Agriculture and manufacturing sectors coupled with a sustained improvement in the services sector. In the oil sector, additional 200,000bpd capacity from Egina oilfield coupled with a lower plausibility of militant attacks guides our surmise of improved output in coming quarters, with expected crude oil production of 2.04mbpd. In the non-oil territory, improved farming activities as conflict in the north moderates, recovery in manufacturing sector following the conclusion of elections and increased active subscribers would lead to an expansion in non-oil output. That said, we expect the Nigerian economy to grow by 2.2% YoY over 2019 (2018: 1.9% YoY).

***In this report, we focus on development in the domestic environment, highlighting our views on the drivers for growth over 2019.***

*Q1 19 GDP: Strong start to the year but not great*

Notwithstanding the material slowdown in the manufacturing sector occasioned by electioneering concerns and contraction in the oil sector, the Nigerian economy expanded by 2.0% YoY in the first quarter of 2019 led by strong outings in the services sector and Agric sector – which combined accounts for 60% of the GDP – to fuel growth in the non-oil space by 2.5% YoY. Suffice to say, while the outturn in the Agric sector (+3.2% YoY) aligned with our surmise, activities in the services sector exceeded our expectation as an unanticipated level of improvement in voice and data subscribers left the output in the ICT<sup>1</sup> sector stronger, with growth at 3.1%. On the flipside, oil sector (-2.4% YoY) contracted for the fourth consecutive quarter, mirroring decline in crude production over the period.

**Figure 1: Growth in Real GDP, Oil, and Non-Oil GDP**

	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	FY 17	FY 18
Agriculture	3.0%	1.2%	1.9%	2.5%	3.2%	3.4%	2.1%
Manufacturing	3.4%	0.7%	1.9%	2.4%	0.8%	-0.2%	2.1%
Services	0.5%	4.1%	3.4%	3.8%	3.1%	-0.8%	3.0%
Construction	-1.5%	7.7%	0.5%	2.0%	3.2%	1.0%	2.2%
Trade	-2.6%	-2.1%	1.0%	1.0%	0.8%	-1.1%	-0.7%
<b>Non-Oil GDP</b>	<b>0.8%</b>	<b>2.0%</b>	<b>2.3%</b>	<b>2.7%</b>	<b>2.5%</b>	<b>0.5%</b>	<b>2.0%</b>
<b>Oil GDP</b>	<b>14.0%</b>	<b>-4.0%</b>	<b>-2.9%</b>	<b>-1.6%</b>	<b>-2.4%</b>	<b>5.5%</b>	<b>1.4%</b>
<b>Real GDP</b>	<b>1.9%</b>	<b>1.5%</b>	<b>1.8%</b>	<b>2.4%</b>	<b>2.0%</b>	<b>0.8%</b>	<b>1.9%</b>

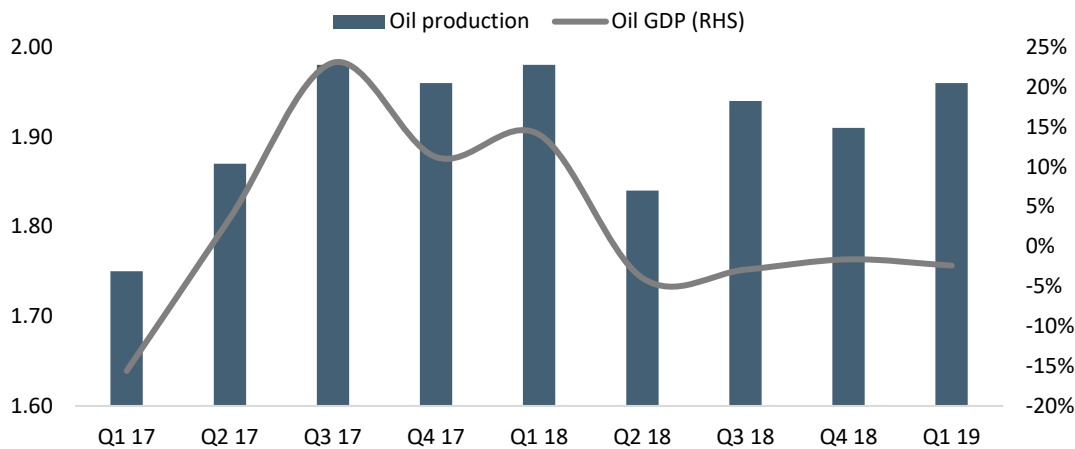
Source: NBS, ARM Research

*Pipeline leakages beset the Oil Sector*

As earlier stated, oil production over Q1 2019 came in lower, following intermittent pipeline leakages. Given that there were no major issues with Trans Forcados – which is the country's key pipeline – we believe the leakages were related to the Nembe Creek Trunk Line with total capacity of 150,000bpd. For clarity, media sources revealed the pipeline was shut for over a week in March following the leakages discovered on February 28 and an eventual explosion on 2nd March 2019. Consequently, production for the period printed at 1.96mbpd – down from 1.98mbpd recorded in Q1 18 – with the sector recording 2.4% YoY contraction.

<sup>1</sup> A subset of the Services sector

**Figure 3: Trend in crude oil production (mbpd) vs oil GDP**

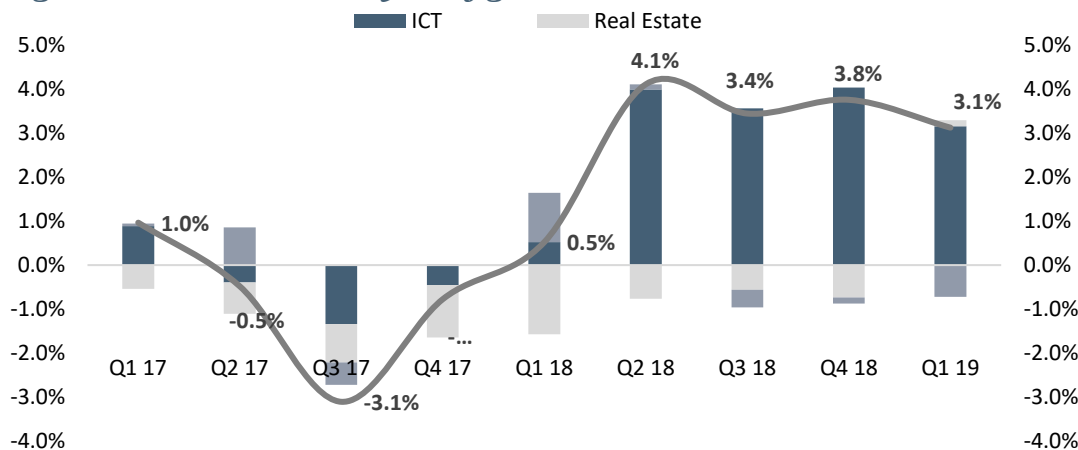


Source: NBS, ARM Research

### ICT and transport sector strengthened services GDP

As stated earlier, the non-oil sector expanded by 2.5% largely emanating from better than expected output in the services sector – grew 3.1% YoY following expansion in telecommunications subsector. For clarity, voice and data subscribers recorded double digit growth over Q1 19 to 173.8 million subscribers compared to 148.3 million subscribers in Q1 18. Largely, with the growth in customers across the sector lower compared to its early growth stage, innovative service delivery now anchors growth in the sector. For context, to grow its data subscriber base, MTN Nigeria introduced the “Double data” plan which allows customers get more data at lower prices, thus, sparking competition across the sector with other players unveiling related plans. Further supporting the output in the services sector is the improvement in road transport (+19.5% YoY) and real estate (+0.9% YoY), which overshadowed the contraction in financial services (-7.6% YoY).

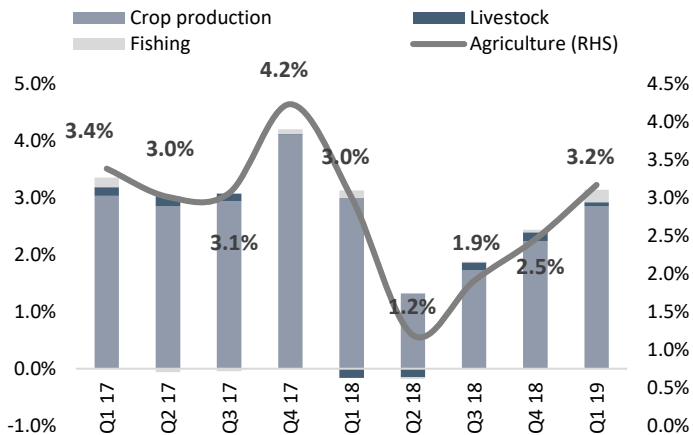
**Figure 1: Attribution analysis of growth in the services sector**



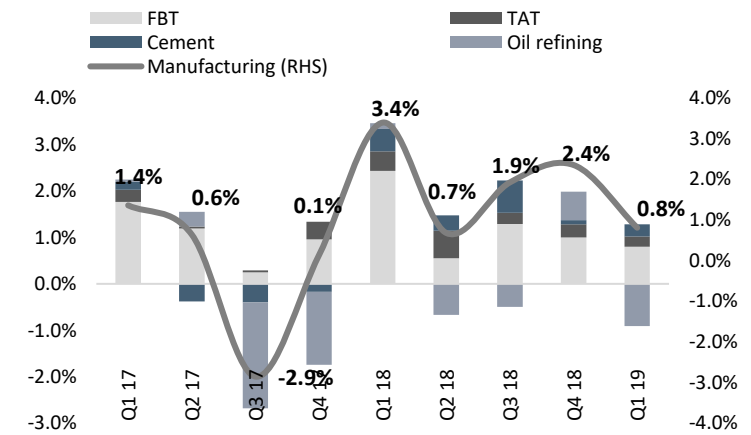
Source: NBS, ARM Research

*Agriculture finds firm footing amidst farmers-herdsmen conflict*

Activities in the agriculture sector picked up in the first quarter of 2019, expanding by 3.2% (Q1 18: 3.0% YoY) driven by improved crop production. To recall, crop production over the last three quarters of 2018 was unimpressive as the conflict between the herders and farmers in North Central and North East curtailed farming activities during the period. However, we stated that a recovery was bound to occur this year, given the critical nature of the sector. True to our words, crop production gained momentum in Q1 19, expanding by 3.3% YoY from an average of 1.9% recorded in the last three quarters of 2018. For us, we believe continued efforts of the government to curb the conflict-induced drain on cultivated and harvested crops drove the overall improvement. Elsewhere, production activities in the manufacturing sector slowed with companies within our coverage recording either a decline or slower growth in revenue – driven by the electoral activities over the period. Diving into the key subsectors, growth in FBT<sup>2</sup> moderated to 1.8% YoY (Q4 18: 2.2%), TAF<sup>3</sup> 1% YoY (Q4 18: 1.2%), while oil refining contracted by 49.6% YoY which together overshadowed growth in cement production of 2.8% YoY (Q4 18: 1% YoY). Accordingly, the sector recorded 0.8% YoY growth (Q4 18: 2.4% YoY; Q1 18: 3.4% YoY).

**Figure 2: Attribution analysis of Agric Sector**

Source: NBS, ARM Research

**Figure 3: Attribution analysis of manufacturing sector**

Source: NBS, ARM Research

Elsewhere, notwithstanding the delayed passage of the 2019 budget, activities in the construction sector expanded by 3.2% YoY in Q1 19. Taking a cue from the listed construction companies like Julius Berger Nigeria Ltd, there were no new projects embarked on during the period which implies the sector expansion largely mirrors completion of previously approved projects. Also, for the third consecutive quarter, trade sector expanded by 1% YoY which we believe echoes mild gains from

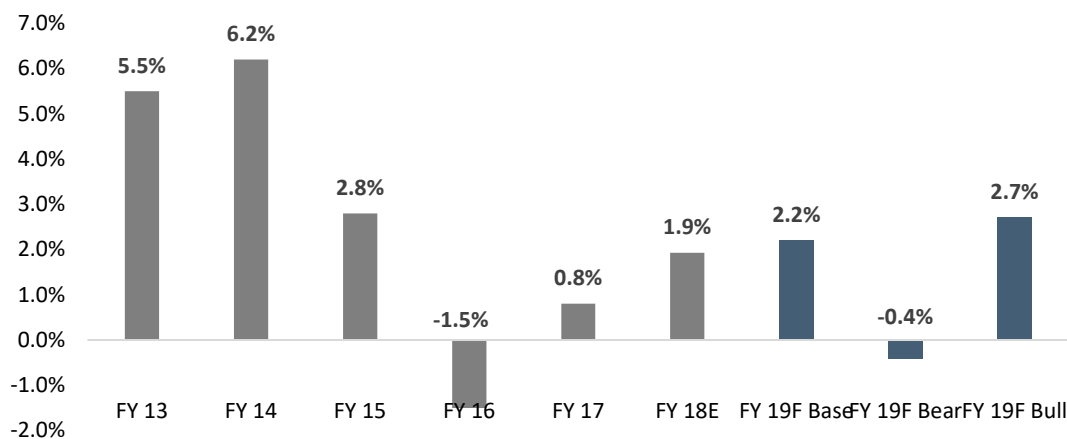
<sup>2</sup> Food, Beverage and Tobacco<sup>3</sup> Textile, Apparel and Footwear

improved FX availability. To buttress, across shelves and markets, we've seen more imported brands in recent times, with some of these goods giving the domestic players a tough time.

### *We expect the economy to grow by 2.2% in 2019*

Coming into 2019, our views on FX stability and expected calmness in the polity post-election had informed our stance of an improvement in economic growth over the year. Notably, we had stated that the growth will be anchored on stronger performance in the non-oil sector as the lower investment in the oil sector – save for the addition of the Egina oil field – amidst shut-ins at key oil exporting pipelines will result in slower growth in the oil sector and by extension a much slower contribution to overall GDP. Notwithstanding, our optimism of stronger contribution from the non-oil sector, we had downplayed the impact of the innovative programmes by key industry players in the ICT on the overall subsector growth. Reflecting the improved activity in the ICT subsector in Q1 19, coupled with recovery in both the Agriculture and manufacturing sectors, we now expect a much robust growth in GDP over 2019 by 20bps to 2.2% YoY (FY 18: 1.9% YoY).

**Figure 4: Annual Real GDP growth**



Source: NBS, ARM Research

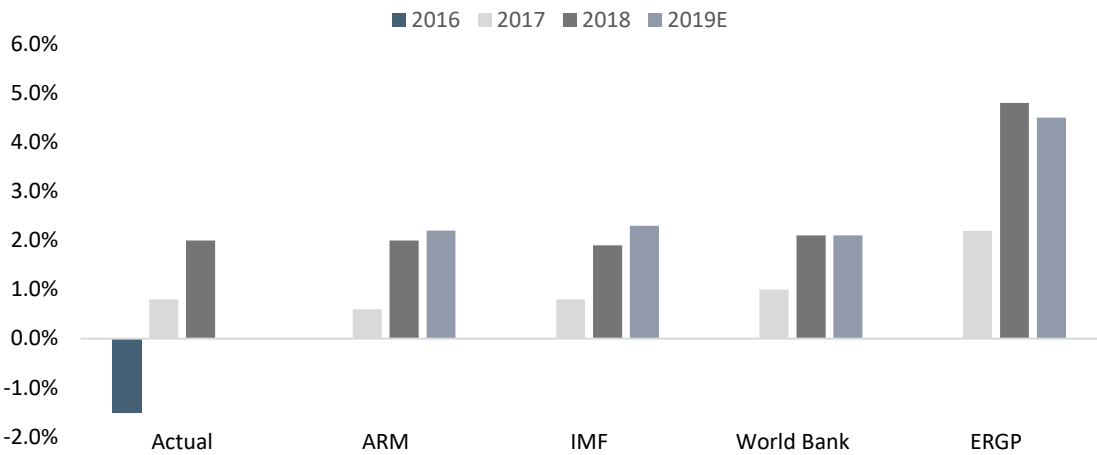
Starting with the harbinger of growth, we retain our surmise on most sub-sectors in the nonoil territory with slight changes to services – driving a nonoil sector growth of 1.8% YoY (FY 18: 2.1% YoY). While we made an upward adjustment to the growth assumption for ICT subsector, the high base of growth in the prior year, the lull in the real estate and slower growth of credit creation in financial services is expected to constrain the rate of growth for the overall services sub-sector. In the ICT subsector, the upward review to our assumption emanated largely from the now telling impact of the innovative customer acquisition programs. For financial services, notwithstanding the recent policies aimed at enhancing

private sector lending – we do not see much traction, as banks remain cautious in growing their risk assets. Lastly, we believe that activities in real estate sector would remain muted given its oversupplied state. That said, activities in services is expected to expand modestly by 1.7% YoY (FY 18: 3% YoY).

On Agriculture, we remain optimistic of a recovery in crop production due to favorable weather and government intervention aimed at curbing ongoing conflict in the northern region. On the government intervention, the RUGA (rural grazing area) settlement program was recently proposed, which requires each state to provide lands for the herders to grow their cattle. Though the program was suspended due to kickbacks from various states, we are positive on some form of concession by the State government given the critical nature of the sector. Further buttressing our point is the ongoing discussions on a peace pact between the Zamfara state government and armed bandits in a bid to improve farming activities in the state. That said, we expect the sector to grow by 3.2% YoY (FY 18: 2.3% YoY). Elsewhere, while the general elections slowed activities in the manufacturing sector, we see some traction in the sector beyond Q1 2019. Further upside would be payment of the minimum wage approved at the start of the year and successful implementation of the presidential order to clear the Apapa gridlock which had been a strain on producers over the last two years due to difficulty in transporting raw materials. That said we expect the manufacturing sector to grow by 2.13% YoY.

In the oil sector, we had highlighted at the start of the year that the plausible risk to crude oil production would be the resumption of militant attacks during the first quarter of 2019 should the electoral process get violent. With militant attacks out of sight, we see no risk to overall production asides minor pipeline leakages. Asides that, additional 200,000bpd capacity from Egina oilfield which resumed operations in January further supports our stance of increased production. For context, while NNPC is yet to provide any data on Nigeria's oil production this year, our channel checks with external sources reveals that actual production touched 2mbpd (condensates inclusive) in April. That said, we expect average oil production to print at 2.04mbpd – 6.4% higher than the prior year. Overlaying the actual Q1 19 numbers with our upward adjustment to the services sector translates to FY 19 growth estimate of 2.2% (Previously 2%), upheld by improvement in both the oil and non-oil sector.

Figure 5: YoY GDP growth forecast (ARM vs IMF, World bank and ERGP)



Source: NBS, IMF, World Bank, Budget Office, ARM Research

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