Nigeria's Economic Outlook

Political Environment | Status Quo to Continue?

During the 3rd quarter of the year 2019, several events occurred in the Nigerian political space.

Firstly, after a long wait, President Muhammadu Buhari formally inaugurated his new cabinet following a successful re-election earlier this year. 43 ministers – substantive and ministers of state, took their oaths.

According to the list, President Buhari maintained his position as Petroleum Minister, a post he has held since 2015. A number of appointees from the last cabinet maintained their portfolios among others, Chris Ngige (Labour and Employment), Geoffrey Onyeama (Foreign Affairs), Babatunde Raji Fashola (Works and Housing) and Abubakar Malami (Minister of Justice). The Nigerian Senate vetted and passed all nominees for appointment. Out of the 43 appointees, seven of them were women.

President Muhammadu Buhari formally inaugurated his new cabinet.

Following a series of xenophobic attacks on Nigerians living in South Africa in 2017 due to the alleged involvement of Nigerians in drug trafficking, prostitution and people trafficking, relationships between the two countries deteriorated. In September 2019 the attacks resumed with the destruction of Nigerian property in Johannesburg. An estimated 120 people were allegedly killed since the attacks started.

Reprisal attacks occurred in Lagos, Nigeria. Nigeria pulled out of the ongoing World Economic Forum in Cape Town and also recalled the Nigerian ambassador to South Africa in protest against the attacks. These attacks have led to analysts reviewing the outlook of the performance of South African companies in Nigeria.

Newly appointed Economic Advisory Council (EAC).

President Muhammadu Buhari has constituted a new Economic Advisory Council (EAC) with members as follows:

1. Prof. Doyin Salami – Chairman

2. Dr. Mohammed Sagagi – Vice-Chairman

3. Prof. Ode Ojowu – Member

4. Dr. Shehu Yahaya – Member

5. Dr. Iyabo Masha – Member

6. Prof. Chukwuma Soludo – Member

7. Mr. Bismark Rewane – Member

8. Dr. Mohammed Adaya Salisu – Secretary (Senior Special Assistant to the President, Development Policy)

P&ID vs Nigera: How Nigeria got hit with a $9.6bn judgment debt in London

On 11 January 2010 Process and Industrial Development (P&ID), a company based in the British Virgin Islands, signed a contract with the Federal Government of Nigeria. In an elaborate report by The Africa Report, this contract is called a gas supply and processing agreement. Nigeria's government agreed that, over a 20-year period, it would supply natural gas (wet gas) to P&ID's production facility.

In return, P&ID would process the wet gas by removing natural gas liquids and return approximately 85% of it to the government in the form of lean gas. This lean gas was to be returned at no cost to the Nigerian government.

Based on this agreement, Nigeria was supposed to arrange for the supply of wet gas to P&ID's gas processing facility which it intended to build in the country's Cross Rivers State. This required the government to construct pipelines and arrange facilities for transporting the wet gas. The government failed to do this for three years.

The $9.6 billion appears to be the largest amount of damages awarded against Nigeria to date.

P&ID viewed this failure as a repudiation of the contract. In simpler terms, this means that the government renounced their obligation under the contract. Consequently, in March 2013, P&ID began an arbitration action against the government before a London tribunal.

Clause 20 of the agreement, which both parties signed, provided that any disputes were to be resolved by arbitration with the seat of arbitration being London, England or any other place agreed by the parties. Nigeria tried to contest this, but its appeal to have the tribunal sit in Nigeria failed.

At the tribunal, P&ID claimed that it had invested $40 million in the project even though it had not acquired the land or built any facilities for gas processing. It claimed damages of about US$6.6 billion dollars: the amount of the net income it would have earned over the 20-year period of the agreement.

In response, the government argued that the damages claimed were not a fair and reasonable consequence of the government's breach of the agreement. This is because P&ID never commenced building the gas processing facility. It also argued that P&ID should be awarded only three years' worth of income as by that time, the company should have found some other profitable investment which would reduce its losses from the breach.

Similarly, the government objected to the measure of estimated expenses and income stream which P&ID used to calculate its damages claim.

The $9.6 billion appears to be the largest amount of damages awarded against Nigeria to date. Evidence however suggests this is not the first time that Nigeria has failed to meet its contractual obligations. In 2016 it was reported that investors in Nigeria's power sector threatened to pull out due to the government's failure to meet its contractual obligations.

This case also demonstrates an ongoing issue with the government's attitude to critical infrastructural projects. The Mambilla hydroelectric power project is a case in point. In spite of the huge potential offered by the project, it has been plagued by several controversies ranging from corruption and embezzlement of funds to the "irregular" awarding of contracts, and a general lack of political will.

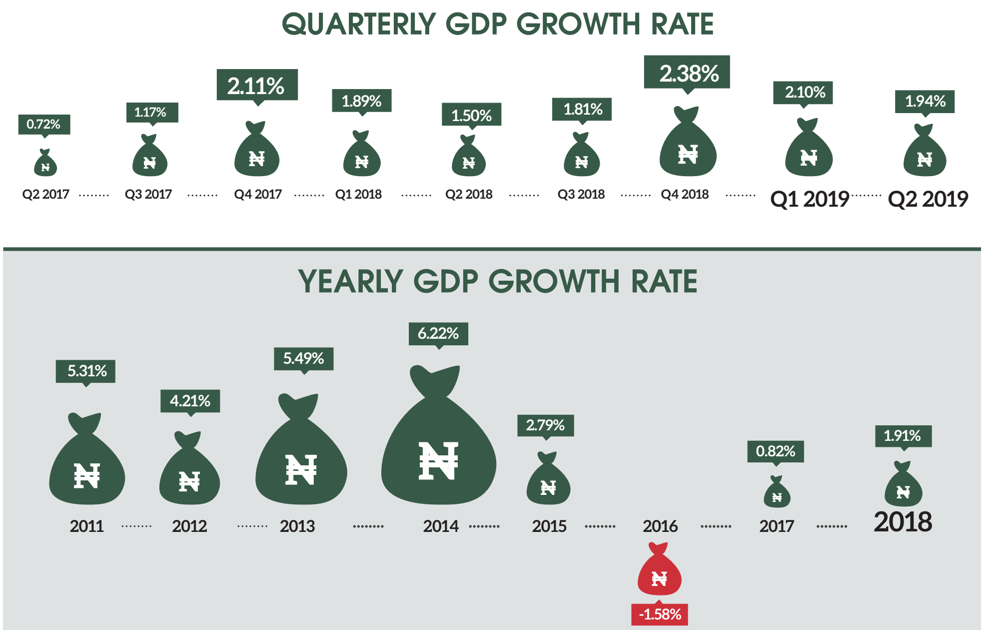
The Nigerian government is yet to pay the judgement debt. Allegations of domestic and international conspiracy surrounding the agreement continue to abound. For now, the government has said that it intends to appeal the amount awarded.

The performance observed in Q2 2019 follows an equally strong first quarter performance

GDP | Decelerating growth: New Fiscal Stimulus Needed?

Gross Domestic Product (GDP) grew by 1.94% (year-on-year) in real terms in the Q2 of 2019 compared to 2.10% (revised from 2.01% due to oil output revisions) recorded in the first Q1 of 2019. This indicates a decline of –0.16% points. On a half year basis, real growth in the first half of 2019 stood at 2.02%, higher than in 2018 which was 1.69%.

Figure 11: GDP Growth Rate (%) 2017- 2019



The performance observed in Q2 2019 follows an equally strong first quarter performance, and was likely aided by stability in oil output as well as the successful political transition.

The Oil Sector recorded in Q2 2019 an average daily oil production of 1.98million barrels per day (mbpd), or 7.6% higher than the daily average production of 1.84mbpd recorded in the same quarter of 2018 but slightly less than output recorded in Q1 2019 (1.99mbpd-revised from 1.96 mbpd). The oil sector posted a real growth rate of 5.15% (year-on-year) in Q2 2019, representing a 9.10% points increase relative to the rate recorded in the corresponding quarter of 2018. It also indicates an increase of 6.61% points when compared to Q1 2019(revised). The sector contributed 8.82% to total real GDP in Q2 2019, up from levels recorded in the corresponding period of 2018 but down compared to the preceding quarter, where it contributed 8.55% and 9.22% respectively.

The non-oil sector grew by 1.64% in real terms during the reference quarter. This was -0.40% points lower than recorded in the same quarter of 2018, and -0.83% point lower than the first quarter of 2019. During the quarter, the sector was driven mainly by Information and communication, Mining and Quarrying, Agriculture, Transportation and Storage, as well as Other Services. In real terms, the Non-Oil sector contributed 91.18% to the national GDP, lower than the share recorded in the second quarter of 2018 (91.45%) but higher than the first quarter of 2019 (90.78%).

A breakdown of the GDP data shows that 6 activities expanded whilst 5 contracted and 8 decelerated.

A breakdown of the GDP data shows that 6 activities expanded whilst 5 contracted and 8 decelerated (slowed). The fastest growing sectors were mainly in services – oil & gas (5.15%), human health (1.13%) and education (0.96%). These sectors contribute approximately 12% to GDP and employ less than 10% of the Nigerian labour force.

Figure 12:

REAL GDP GROWTH RATE OF OIL AND NON-OIL SECTORS

NON-OIL GDP

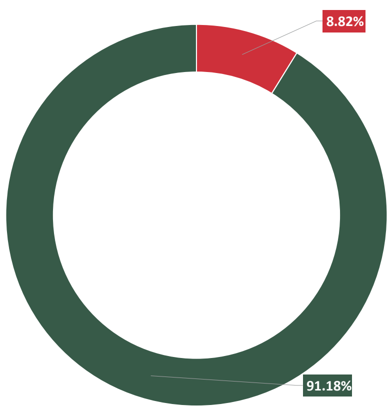
Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019
90.45	91.45	90.62	92.94	90.78	91.18

OIL GDP

Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019
9.55	8.55	9.38	7.06	9.22	8.82

Figure 13:

CONTRIBUTION OF OIL AND NON-OIL SECTORS



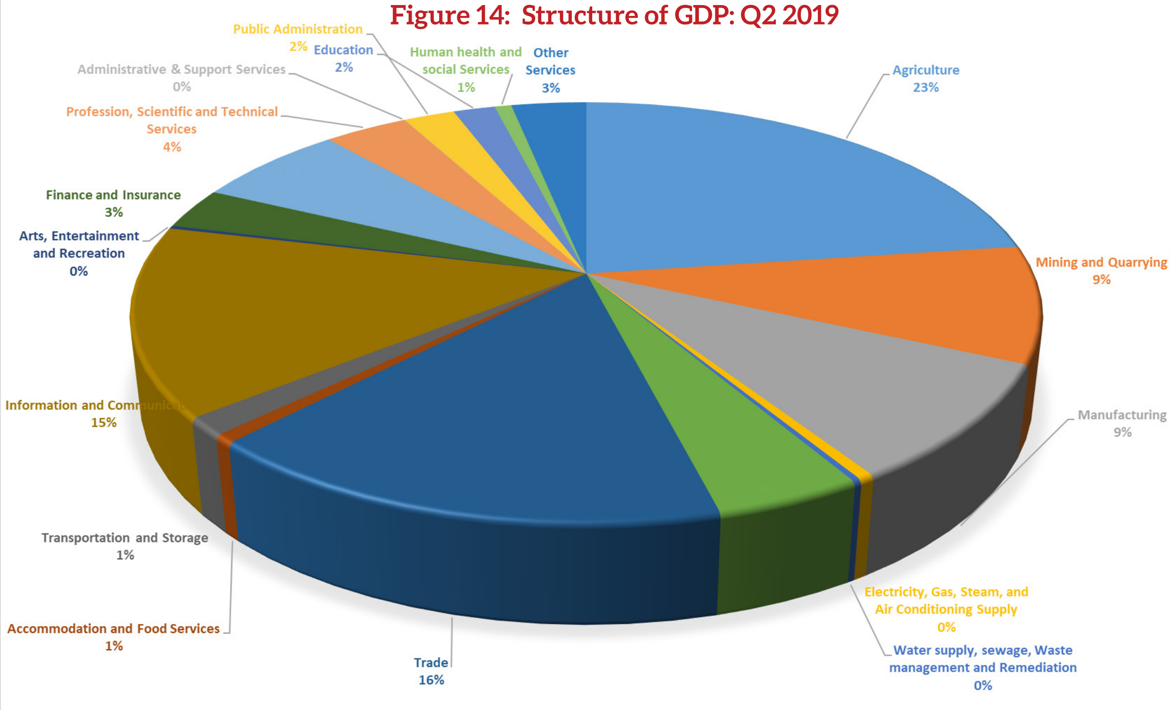
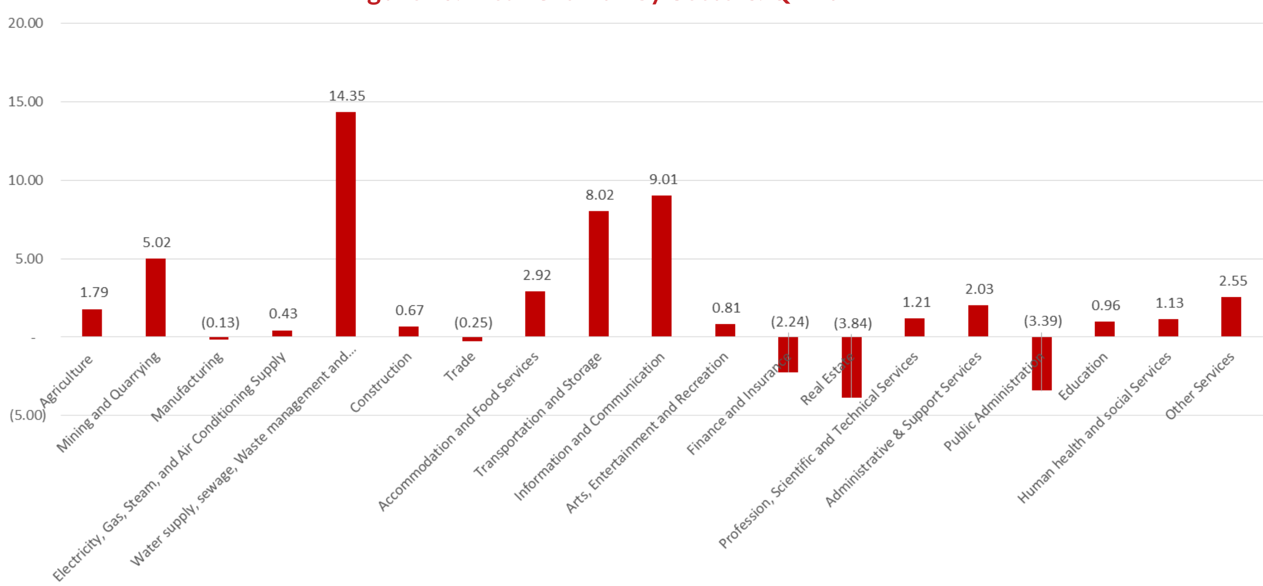


Figure 14: Structure of GDP: Q2 2019

The decelerating sectors are also interest rate sensitive and employment elastic - agric (1.79%) and construction (0.67%). This lukewarm performance was largely due to seasonal factors. Q2 is usually the planting season of most agric commodities, thereby creating scarcity and pushing up prices. The rainy season also commenced in Q2 and slowed construction activities.

The sectors with negative growth include - manufacturing (-0.13%), trade (-0.25%), and real estate (-3.84%). These sectors employ more than 30% of the labour force.

Figure 15: Real Growth by Sectors: Q2 2019



Source: NBS

The weak Q2 GDP growth indicates that the economy is in need of a fiscal stimulus. This should be the focus of the fiscal team as they formulate the 2020 budget and the medium term policy framework. The fiscal catalyst however needs to be supported by growth stimulating monetary policy.

The harvest season for most commodities is the third quarter of the year. This should have a positive impact on agricultural outputs thereby impacting GDP positively. Also, as the newly formed cabinet sets out to implement the 2019 budget, the construction and real estate sectors also stand to benefit from capital spend. Therefore, we expect a marginal increase in Q3 GDP growth.

Inflation | Core Inflation to Continue Declining but Approaching an Inflection Point

Inflation increased by 11.02% (year-on-year) in August 2019 compared to 11.08% in July and 11.22% in June.

The continued fall in inflation was partially as a result of harvesting and declining consumer disposable income. This is the 3rd consecutive monthly decline and the lowest level since February 2016.

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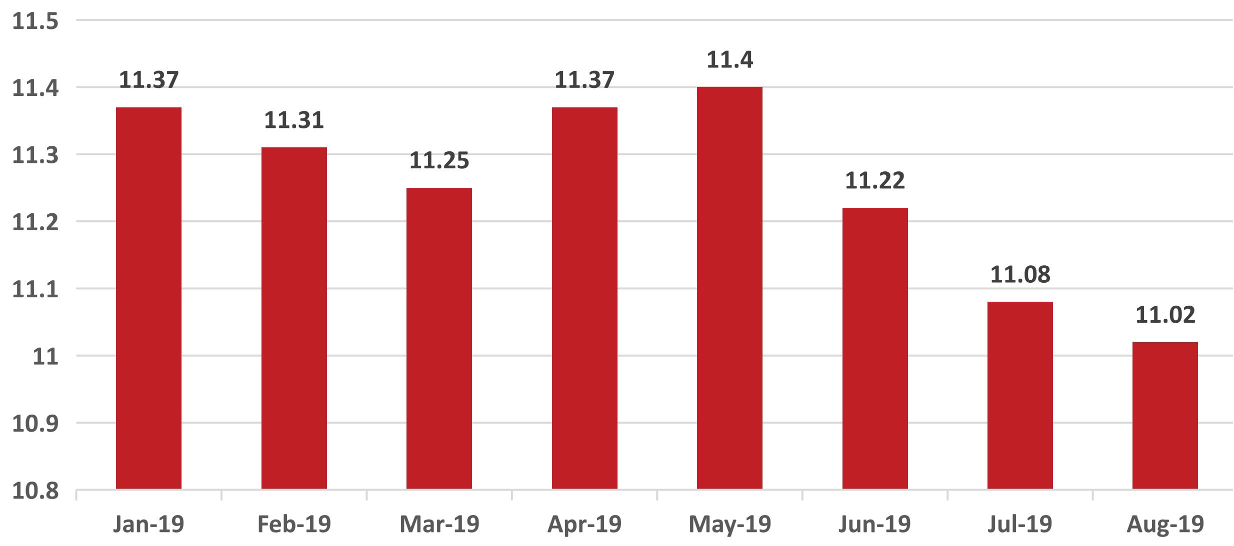
Decelerating inflation continued in August 2019 despite several pronouncements regarding restrictions on the import of some food items, minimum wage and the recent border closures. The impact of these restrictions was a spike in the prices of food items. The price of a 50kg bag of rice increased by almost 30% to N18,000 in August from N14,000 in

Figure 16: Inflation Rate (%) Jun 2018. - Aug. 2019



Source: NBS, SAMTL RESEARCH

July. It however curtailed smuggling of petrol and diesel, thus creating excess supply and driving down prices. The wholesale price of diesel fell by 3.15% to N215/liter.

It is expected that inflationary pressures will be re-ignited as a result of increased seasonal demand, the implementation of the minimum wage policy, adjustments in the exchange rate for computing custom duty to N326/$, and forex restriction for dairy products and general food imports.

Foreign Trade | Imports growth far outpaces exports growth

According to the National Bureau of statistics (NBS), Nigeria's total foreign trade (value of exports and imports) grew by 4.42% to N8.60 trillion in the second quarter (Q2) of 2019, from N8.24 trillion recorded in the previous quarter (Q1). Combined with the Q1 2019 performance, the value of total trade as at half year 2019 was 15.43% higher than for the same period in 2018.

The NBS noted that the performance of Nigeria's trade for Q2 was largely as a result of stronger growth in the value of imports far outpacing growth in the value of exports which rose only marginally.

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Exports

The value of total exports in Q2 2019 increased by 1.34% against the level recorded in Q1, 2019 and 2.06% when compared with its value in Q2, 2018.

Exports by sectors show that crude oil export accounted for almost 90% of Nigeria's total export in Q2 2019. Crude oil export in Q2 was estimated at N3.9 trillion, from N3.3 trillion recorded in Q1 2019.

The value of Agricultural exports in Q2 was 14.66% lower than in Q1 2019. In Q1 2019, Agricultural goods exports were estimated at N73 billion, as against N86 billion in Q2.

The value of Raw material exports was 14.52% lower than the value in Q1 2019 and 1.71% lower than in Q2 2018.

The value of Solid mineral exports declined by 15.53% compared to Q1 2019 and 62.27% against the corresponding quarter in 2018.

Also, the exports of Energy goods dropped by 12.31% in value compared to Q1 2019 and 15.15% when compared with Q2 2018.

Lastly, the value of manufactured exports decreased by 77.05% when compared with the value recorded in Q1 2019. In Q1 2019, Nigeria exported N462 billion worth of goods, while the value dropped significantly to N462.2 billion in Q2.

Nigeria's Major Export Trading Partners in Q2 2019 were India (17.27%), Spain (11.97%), Netherlands (10.41%), United States (7.68%), and France (6.09%)

Imports

In Q2 2019, Nigeria's imports constituted 74.52% of manufactured goods. A total of N2.47 manufactured goods was imported into the country. Specifically, the value of imported manufactured goods decreased by 10.86% in Q2 2019 against the value recorded in Q1 2019.

The value of imported Agricultural products was 5.79% higher in Q2 2019. Basically, the country imported N249.9 billion worth of agricultural goods.

Also, the raw material was one of the major goods imported into the country in Q2 estimated N346.4 billion. In total, Nigeria's raw material imports grew 4.97% over the value recorded in Q1 2019.

Similarly, the value of Solid minerals imports was 63.46% higher than in Q1, 2019 and 68.34% higher than the value recorded in Q2 2018.

Lastly, the value of energy goods imports was 74.65% lower than in Q1, 2019.

Major Import Trading Partners in Q2 2019 were China (25.47%), United States (10.53%), Netherlands (9.33%), India (7.48%), and Belgium (6.21%).

Capital Inflows & Outflows

Capital imports into Nigeria declined by 31.4% to $5.8bn in Q2 2019 from $8.49bn recorded in the previous quarter Q1 2019. Of the three components, Portfolio Investments accounted for the largest value of $4.29bn (73%) followed by Other Investments at $1.30bn (22.41% of total capital importation) and Foreign Direct Investment at $222.89mn (3.83%).

A further breakdown of the report showed that the largest source of capital investment into Nigeria was the United Kingdom ($3.13bn) followed by the United States ($1.15bn), the United Arab Emirates ($344mn) and South Africa ($314mn). Three of the top four countries are currently experiencing uncertainties.

The United Kingdom's Brexit plan still remains unclear, while the trade war and incidents of xenophobia in the US and South Africa respectively could

These developments could limit the capital imports originating from these countries in subsequent quarters.

slow growth in both countries with ripple effects on the regional and global economy. These developments could limit the capital imports originating from these countries in subsequent quarters.

Monetary Policy | Status Quo maintained

The CBN Monetary Committee left all parameters unchanged in the quarter Q3 2019. The MPR remained at 13.50%; CRR at 22.5%; Liquidity Ratio at 30.00%; and Asymmetric Window at +200 and -500 basis points around the MPR.

Broad money supply grew by 1.36% to N28.27trn in July. In August, M2 growth was supported by an increase in the loan to deposit ratio (LDR), higher FAAC disbursement and net OMO inflows. FAAC allocation and net OMO bills amounted to N1.56trn (5.51% of broad money supply). In a bid to boost lending to the private sector, the CBN raised the LDR by 3% to 60% and reduced SDR to N2bn. This has compelled banks to increase lending, and do so at competitive rates.

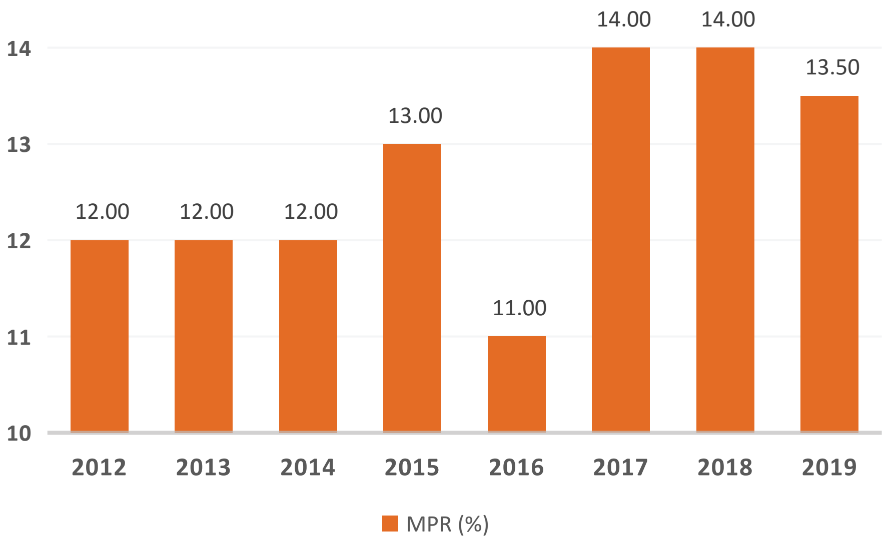
The CBN Monetary Committee left all parameters unchanged in the quarter Q3 2019.

A significant enough spike in inflation could make the MPC change its stance from the tight situation to further tightening in November.

Foreign Exchange Market | Naira remains Stable

The Nigerian forex market is segmented with multiple exchange rates. The most important rate is the Investors and Exporters window (IEFX). No less than 55%-60% of Nigerian forex transactions are traded on this window. The CBN and most exporters and investors use this window. It serves not only

Figure 17: Monetary Policy Rate (%) 2012 - 2019



Source: : CBN, SAMTL RESEARCH

as a source of price discovery but also a barometer for measuring potential and actual CBN intervention in the market. Some of the exchange rate determinants are balance of payments, capital inflows and trade balance.

At the parallel market, the naira temporarily appreciated against the dollar to N359/$ on August 2nd before retreating to close the period Q3 2019 at N360/$. The apex bank intervened with a total of $787.96mn in August, 35.04% lower than $1.21bn sold in the corresponding period in July. Whilst the currency strengthened against the pound to close the period Q3 2019 at N445/£, it traded within the band of N396-398/€ against the euro.

At the interbank market, the naira depreciated by 0.16% to close at N306.95/$ on September 2nd. In the same vein, the currency weakened by 0.14% to close at N362.73/$ at the IEFX window. Total forex traded increased to $6.87 billion compared to the total of $4.68 billion in the corresponding period in July.

The restriction of forex access for food imports coupled with demand pressures from the payment of tuition fees would weaken the Naira at the parallel market. However, the naira is expected to trade between N361-N363/$ at the parallel market in the coming weeks as the CBN continues to intervene in the forex market.

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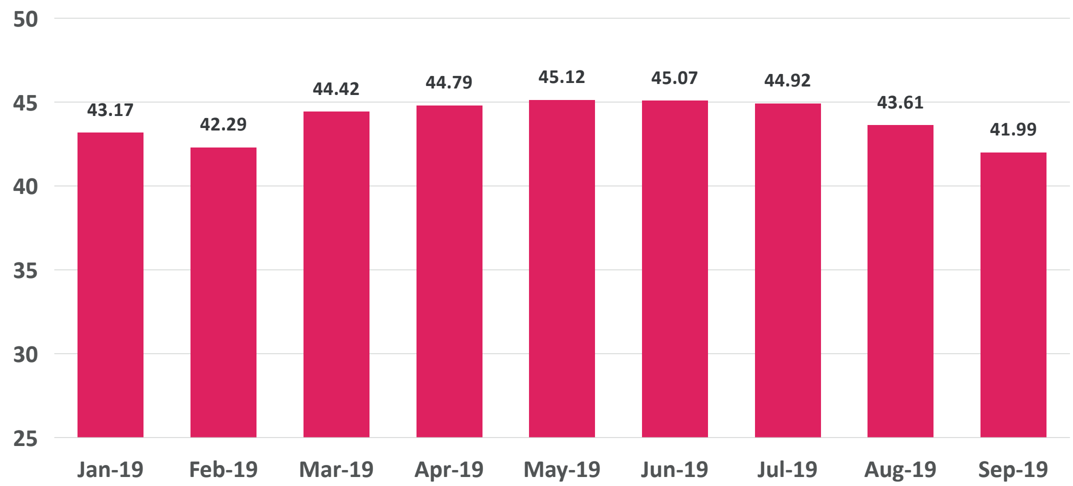
A depreciation of the currency is negative for sectors such as manufacturing that depend mainly on imported inputs.

Foreign Reserve | External Reserves Slides

Nigeria's gross external reserves has continued its downward trend since the beginning of the review period. It declined by 3.39% to close the period Q2 2019 at $43.36bn compared to $44.88bn on August 1st. Subsequently,

Figure 18: Foreign Reserves ($'bn) Jan 2019. - Sept 2019.



Source: NBS, AAML RESEARCH

Nigeria's import cover has dropped to 10.80 months from 11.17 months on August 1.

The expectation of the CBN to intervene in the foreign exchange market to defend the currency from demand pressures would negatively affect the external reserves. Therefore, Nigeria's external reserve may decline further to between 42-43 billion dollars.

A decrease in the level of external reserves will affect the CBN's ability to intervene with the currency, which will reduce the country's buffers against negative external shocks.

FAAC

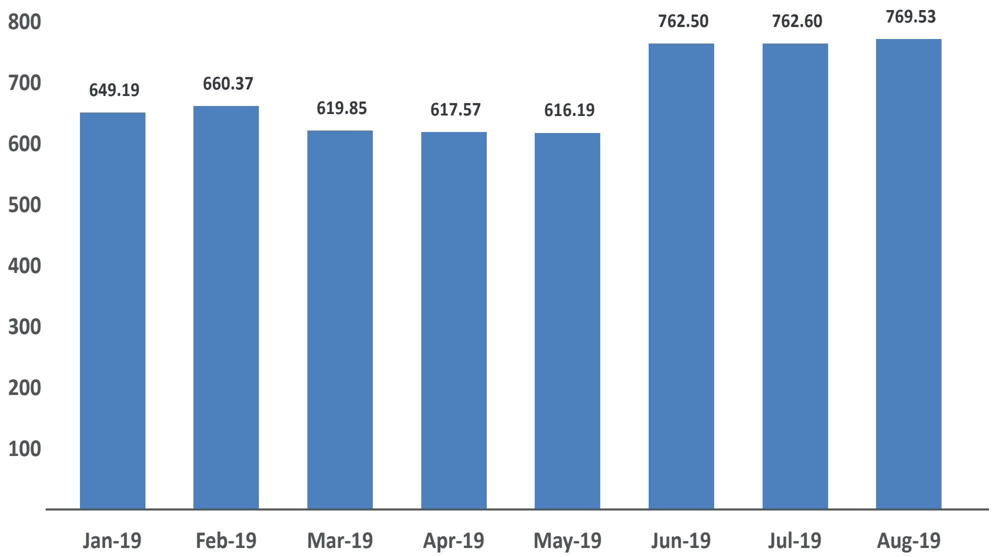
The Federation Account Allocation Committee (FAAC) disbursed the sum of N769.53bn to the three tiers of government in August 2019 from the revenue generated in July 2019. The amount disbursed comprised of N607.37bn from the Statutory Account, N94.16bn from Valued Added Tax (VAT) and N999.99m exchange gain differences.

Federal Government received a total of N299.80bn from the N769.53bn. States received a total of N190.38bn and Local Governments received N143.57bn. The sum of N51.63bn was shared among the oil producing states as 13% derivation fund. Revenue generating agencies such as Nigeria Customs Service (NCS), Federal Inland Revenue Service (FIRS) and Department of Petroleum Resources (DPR) received N5.70bn, N11.14bn and N5.02bn respectively as cost of revenue collections.

The Federation Account Allocation Committee (FAAC) disbursed the sum of N769.53bn to the three tiers of government in August 2019.

Further breakdown of revenue allocation distribution to the Federal Government of Nigeria (FGN) revealed that the sum of N241.81bn was disbursed to the FGN consolidated revenue account; N5.43bn shared as

Figure 19: FAAC (N'BN) Jan 2019- Aug 2019



Source: NBS

share of derivation and ecology; N2.72bn as stabilization fund; N9.13bn for the development of natural resources; and N6.30bn to the Federal Capital Territory (FCT) Abuja.

The Federation Account Allocation Committee (FAAC) disbursed the sum of N762.6bn to the three tiers of government in July 2019 from the revenue generated in June 2019. The amount disbursed comprised of N652.95bn from the Statutory Account, N108.63bn from Valued Added Tax (VAT) and N1.02bn exchange gain differences.

Federal Government received a total of N309.43bn from the N762.60bn. States received a total of N201.16bn and Local Governments received N151.38bn. The sum of N38.70bn was shared among the oil producing states as 13% derivation fund.

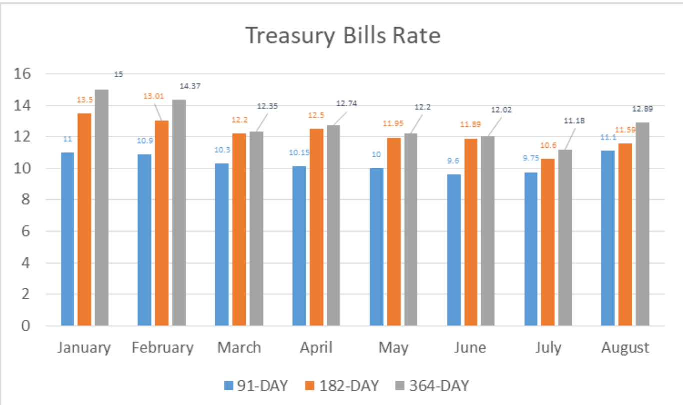
Increase in FAAC in the last quarter can be attributed to higher gross statutory revenue and excess crude account now at standing at $274.41 million. Nonetheless, FAAC is projected to decline in subsequent months due to lower oil revenue, and the FGN's committee set up to recover the N614bn bailout funds given to states.

Money Market | Increased market illiquidity

Average liquidity within the banking system in August was N92.45bn, 71.67% lower than the average of N326.38bn recorded in the corresponding period in July. Within the review period, the market witnessed five consecutive days of negative opening position. The decline in liquidity within the money market could be partly due to the CBN's regulatory measures deadline of September 30.

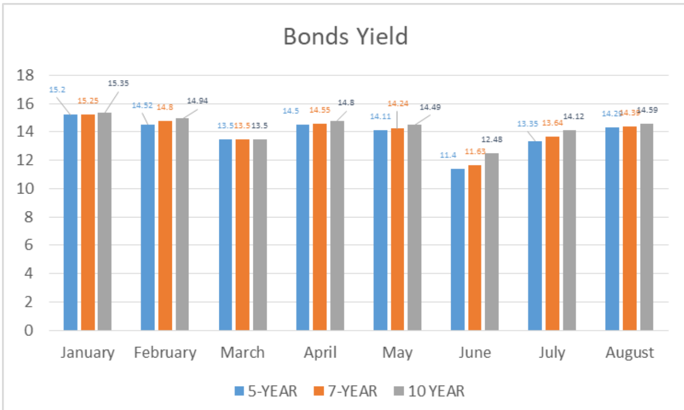
In response to the illiquidity, the NIBOR (OBB/ON) rates leaped up to a 4-month high of 28.29% pa and 30.29%pa respectively on August 19, before retreating to close the period at 8.86%pa and 9.86% pa respectively on September 2nd.

Figure 20: Treasury Bills Rate Jan. - August 2019.



Source: CBN

Figure 21: Bonds Yield Jan. - August 2019.



At the secondary market, all the yields moved in the same direction at an average of 314.33ps while at the primary market, they moved in different directions. The 91-day tenor declined by 5bps while the yields for the 91-day and 364-day tenors inched up by 78.5bps. The Nigerian Inter-Bank Treasury True Yield (NITTY) rates increased across all the three tenors by an average of 342.67bps.

There is likely to be illiquidity in the banking system as the Central Bank of Nigeria (CBN) ordered banks to give out a minimum of 60% of their deposits as loans by September 30, 2019. Therefore, this puts pressure on banks to meet up with this goal in order to refrain from facing sanctions.

Equities Market | Poor performance continues

The NSEASI ended Q3 2019 in the negative territory with -7.80% loss as against -3.46% loss in Q2 2019 and -1.24% loss in Q1 2019.

The Nigerian Stock Market closed the month of September 2019 in the positive territory as market halts the negative sentiment witnessed in the last three months. The NSEASI inched up by +0.38% to close at 27,630.56 points as against -0.69% loss recorded in the month of August 2019.

The NSEASI ended Q3 2019 in the negative territory with -7.80% loss as against -3.46% loss in Q2 2019 and -1.24% loss in Q1 2019.

The continued poor performance in third quarter despite the marginal gain of 0.38% in September, was attributed to post-election uncertainties that continue to trail the economy, as well as the weak Q2 corporate earnings, lack of economic direction, with government delaying the reconstitution of the Federal Executive Council, among others. There was also the effect of the gloomy global economic outlook.

The marginal rebound in September, may also be connected with the low price attraction of most stocks, ahead of their year-end score-card, a situation that has gradually triggered demand for blue-chip stocks now selling at considerable discount to Book Value.

Topping the sectoral index movement table for the period was the NSE Oil/Gas, which rose by 20.63%, thereby outperforming the overall market's All Share index that closed high at 0.38%, followed by the 8.56% gain by NSE Insurance; even as the NSE Consumer goods and NSE Banking could only rise by 7.85% and 7.10% respectively.

Market fundamentals are expected to change in the last quarter of the year. The recent rate cut in developed economies and markets, may likely redirect the flow of funds to emerging market like Nigeria, even as implementation of the 60% minimum Loans-Deposits ratio by the deposit money banks, implementation of the 2019 capital budget and end of year activities could give the market the needed liquidity boost. This is expected to impact equity prices because the market indices in Q4 have always risen by 1.8% on the average over the past 22 years.

NSI ASI JAN. - SEPT. 2019