May 2020

THE INVESTOR

Macroeconomic Review and Market Update

AfriKnowledgeBank

Watching Africa Move

info@afriknowledgebank.com | www.afriknowledgebank.com

AT A GLANCE…

In summarising the first quarter of the year, one cannot ignore the severe impact of the coronavirus outbreak on economic activity. The rightful decision to impose social distancing measures to reduce the spread of the virus has come at a great cost. According to estimates by Mckinsey & Company, the Nigerian economy is projected to contract by almost 3.5% in 2020, a six-percentage point decline relative to pre-COVID-19 projections. To complicate matters, the sharp decline in oil prices magnified the vulnerabilities of Nigeria as the government struggles to finance the 2020 budget. Thankfully, the IMF Executive Board approved $3.4billion emergency financial assistance under the Rapid Financing Instrument to support the economy in addressing the economic impact of the coronavirus. The emergency financing brings a slight relief as Nigeria's oil and gas exports (84% of total exports) are expected to fall by more than $26.5billion (according to the IMF).
This report highlights some of the monetary and fiscal policies directed at supporting economic growth during this period and the performance of various asset classes over the past month.

GDP growth as of Q4 2019		+2.55%	
Inflation as at March 2020	Month-on-Month %	Year-on-Year %	12 Month Avg.Chg%
CPI Inflation	0.84	12.26	11.62
Food Inflation	0.94	14.98	14.11
Core Inflation	0.81	9.73	9.11

*source: NBS

FX Reserves (US$ bn)	**Close**	**1M%**	**3M%**
As at 28/04/2020	$33.44	-5.84	-12.26

*Source: Central Bank of Nigeria

According to the IMF, Nigeria's oil and gas exports (84% of total export) are expected to fall by more than $26.5billion

Closing IEFX Rates

GBP/NGN	488.54	-1.04%
USD/NGN	387.39	0.22%
EUR/NGN	424.06	0.49%

*Source: Bloomberg, data as at 30/04/2020

NSE ASI Statistics as at 30/04/2020	
Current	23,021.01
Previous	22,868.40
Day Change	0.67%
YTD Return	-14.24%
YTD High	29,710.56
YTD Low	20,669.38
52wk High	31,477.51
52wk Low	20,669.38

*Source: NSE

Fixed Income Mark-to-Market	Tenor	TTM	Yield%
Nigerian Treasury Bill	364D	287D	3.9
8.50% FGN 20-NOV-2029	10yr	9.56Y	11.28

*Source: FMDQ as at 30/04/2020

MACRO POLICIES

Monetary Policy

The Central Bank of Nigeria (CBN) is known for juggling interest, inflation, and exchange rate simultaneously to stimulate growth. Either through 'currency adjustments' or 'rebasing of GDP, the CBN has consistently worked towards maintaining Nigeria's status as the '*largest economy*' in Africa. Prior to the pandemic, the projection of oil revenue made authorities confident about having enough FX reserve to support the exchange rate while focusing on increasing economic activity, lowering debt servicing costs (through lower interest rates), and meeting their target of a single-digit inflation rate.

Unfortunately, the sharp decline in oil prices, remittances from abroad, and dwindling foreign interest in CBN's OMO bills have restrained capital inflows. By March, foreign portfolio holdings had declined by 46%* since the beginning of the year and by almost 60%* since mid-2019. As a result of the above, the CBN has witnessed an 13.2% decline in reserves ($38bn in January 2020 to $33bn April 2020*).

FX Policies.

Following the decline in foreign reserves and the significant drop in oil price, the CBN against all odds (who had promised earlier in the year that a devaluation was not going to happen soon) was forced to adjust the exchange rate to Foreign Portfolio Investors (FPIs) from N366.70 to N380.20, a move which we believe will slowly take the Naira towards a "*fairer equilibrium*." By this, we mean that more currency adjustments (i.e., devaluations) that will reflect Nigeria's economic situation are likely to happen in the short to medium term.

Given the gradual easing of the Covid-19 lockdown, the CBN announced the resumption of foreign exchange provision to all commercial banks for onward sales to school fees related payments and SMEs wishing to make essential imports needed to revamp economic activities. In particular, the CBN is resuming the provision of over $100 million per week for those causes. As rationing foreign exchange could have damaging consequences on investor confidence, the CBN will be more flexible, and FX interventions will be limited to smoothing large fluctuations in the exchange rate.

Monetary Policy Rate (MPR)

At the March (Monetary Policy Committee) MPC meeting, the CBN decided to retain the MPR at 13.5%. The decision made was out of a fair argument that increasing the policy rate will reduce money supply and limit DMBs credit creation capacity, thus increasing the cost of credit, with an adverse impact on output growth. In contrast, a reduction in the policy rate will result in massive pressure on inflation, reserves, and exchange rate with damaging effects on growth.

Therefore, the CBN has decided to allow the announced fiscal stimulus to permeate the economy before deciding on further supporting monetary policy measures to boost and strengthen the economy. Other policy rates were also retained.

MPR	Retain at 13.5%
Asymmetric Corridor	+200/-500 basis points around the MPR
CRR	Retain at 27.5%
Liquidity Ratio	Retain at 30%

*Data from CBN

Our Outlook

The IMF's executive board recently approved an emergency fund of $3.4bn to Nigeria. This financial support will help limit the strain on international reserves; however, this will only be useful in the short run to mitigate the sharp fall in global oil prices. If oil prices do not recover in the short term, the CBN may be encouraged to either increase interest rates on OMO bills (to foster an increased inflow of foreign capital) or devalue the currency to relieve some pressure on reserves.

The next MPC meeting is scheduled to hold on the 25th of May.

*Data from CBN

Fiscal Policies

In line with the need for fiscal stimulus to support the economic downturn caused by the COVID-19 pandemic, a N500bn Covid-19 crisis intervention fund has been set up to help cover the cost of the much-needed medical equipment, medicine, and public works programs. In addition to this, a temporary fiscal support package, "Economic stimulus Bill 2020," was announced. The package includes income tax relief equal to a 50% rebate on payroll tax for employees, import duty waivers for medicine and medical goods, reduction in regulated fuel prices, and elimination of fuel subsidies, amongst others.

Although the other fiscal measures have not been costed (as at the time of this report), the federal government announced that the overall government fiscal deficit for 2020 would widen to 6.8% of GDP (from 4.6%** expected before the Covid-19 outbreak). Furthermore, due to the sharp decline in projected oil revenue, the benchmark oil price has been adjusted down to $30 from $57 per barrel, and total revenue is projected to decline by 3.6%** of GDP.

According to the IMF, Balance of Payment gap for 2020 is estimated at $14billion, of which the federal government's recently approved $3.4billion IMF emergency support will cover about 24% of the gap. Also, the authorities are actively engaged in negotiations with the World Bank, the African Development Bank, Islamic Development Bank, and Afreximbank for budget support loans of about $3.6 billion**. The rest of the financing gap is expected to be met by further reserve drawdown and greater exchange rate flexibility.

Fiscal Policy Outlook

The assistance from the private sector has helped ease the financial burden on the federal government. On the 4th of April 2020, the contribution of Nigeria's private sector coalition against COVID-19 hit 15.3 billion Naira with more still underway.

Although we know that coronavirus will dictate government spending in the next couple of months, it is difficult to predict the direction of fiscal deficit. The gradual easing of the lockdown before necessary may lead to an increased number of domestic infections, which would put tremendous pressure on the health care system and business activities. Under that scenario, the fiscal and external financing needs will be larger. In a situation where cases decline and the virus is eradicated, the federal government may continue its revenue-based fiscal consolidation program, which started this year by increasing the VAT rate.

In the future, we expect the government to revisit its tax system to increase government revenue and avoid the CBN financing its deficits.

*Data from FGN Press Release
**Data from IMF Report

ASSET CLASSES

Equities

Past performance is not a reliable indicator of future returns. When investing in overseas markets, changes in currency exchange rates may affect the value of your investment.

With the Nigerian stock markets only just recovering from the 2016 recession, the equities market has experienced a large decline. We are aware that cheap valuations are not a sufficient reason for the market to rally, however, the opportunities for decent returns are vast.
The Coronavirus pandemic has sent the NSE ASI to new lows. The ASI dipped by -14.24% to 23,021.01 as at close of market 30/04/2020. For April, 2020 all other indices finished higher with the exception of NSE Oil & Gas index, and NSE Industrial Goods, which depreciated by 2.84%, and 2.86% respectively*.
The Financial Services industry (measured by volume) led the activity chart with 809.957 million shares valued at N5.666 billion traded in 9,533 deals, thus contributing 80.06% and 57.28% to the total equity turnover volume and value respectively*.
We predict continuing volatility in the short-term as sentiments and technical factors drive the market amidst the pandemic.

Sector Winners and Losers
Looking forward, determining the stocks that will be good is a question of the companies that can operate digitally and drastically reduce capital expenditure. A current trend around the world now is CEOs realizing that remote working is possible, a phenomenon that was previously unheard of in Nigeria.

Moreover, the pandemic has shed light on what the essential sectors are. In Nigeria, those could be thought of as the Telecommunications, Agriculture, and Health industry. For one, the demand for telecommunications is greater as more people work from home. Secondly, the previously underrated Agriculture is now critical as people bulk buy food items - we may see more banks lending companies in this sector. Thirdly, the below-standard health sector is likely to see improved infrastructure as a result of the pandemic.
We believe oil and gas earnings will continue to experience significant pressure until demand picks up, and cost-effective supply is available.

Performance by Sector

30/04/2020	Week Close	MTD Chg%	YTD Chg%
NSE-Banking Index	271.57	15.14	-23.90
NSE Consumer Goods Index	371.12	14.02	-37.40
NSE Oil/Gas Index	209.13	-2.84	-20.34
NSE Industrial Goods Index	1,012.59	-2.66	-5.86
NSE Insurance Index	121.88	2.08	-3.13

*Source: NSE

*Data from NSE

Fixed Income

The economy has seen a rise in default expectations. Fitch Ratings Agency downgraded Nigeria to a 'B' with a negative outlook. The downgrade was mostly due to the decrease in Nigeria's external reserve, which is expected to fall further with the crash in oil prices below $30 per barrel.

Rating Agency	Rating	Outlook
Fitch Ratings	B	negative
Moody's Investors Service	B2	negative
Standard & Poor's	B-	-

Spreads on 30-year Eurobond yields have widened by 600 basis points while domestic bond yields remain low, and for lower maturities, at rates well below inflation.

***Attractive yields on Eurobonds*:** As of 29 April 2020, according to the report issued by DMO, Nigerian Eurobond yield for 2021 maturity reached 15.92% compared to the 7% yield at issue due to foreign investors fleeing the market and waning investor confidence. Yields across other maturities averaged 12%, *which we believe presents a significant buying opportunity*, especially for local investors looking for attractive yields in foreign currency. Investors should, however, be cautious about the risk of default due to pressure on the country's foreign reserves.

Money market (T-bills) yields get "uglier": Late last year, we saw all sorts of reports in the news about the real yields on Nigerian T-bills falling into the negative zone and being the lowest since April 2016. But little did we know that it was just the beginning of the downturn. We saw T-bill rates in the range of 2% to 4% in April. These rates have remained low since the beginning of 2020 and have been the lowest ever seen since 2010. With inflation at 12.2%, investments in these securities currently have negative yields in real terms.

FGN bonds: Bonds remained relatively attractive and stable in April with yield to maturities ranging from 12% to 16%

Although the fiscal and monetary stimulus provided by the authorities makes a long-lasting recession less likely, the downside of the stimulus is the large deficits it implies for the future. In the short term, we expect foreign investors' participation and liquidity levels to continue influencing the fixed income market.

Commodities

The headline of the first quarter has been the collapse in crude oil prices. The commodity witnessed a double attack from demand and supply. The coronavirus outbreak led to reduced demand. On the other hand, major oil producers chose to ramp up supply in the face of falling consumption. Although cheap oil prices are good for the firms and households who rely heavily on petroleum products, it is not good news for oil producers who struggle to produce at a cost below current prices.

MARKET DATA – Week Close 30/04/2020

Top Five Performers

Company	Close	Gain (N)	% Change
ARDOVA PLC	11.5	2.00	20.94
LASACO ASSURANCE PLC	0.27	0.03	12.50
U A C N PLC.	6.90	0.70	11.29
VITAFOAM NIG PLC	4.96	0.45	9.98
CHAMS PLC	0.23	0.02	9.52

*Source: NSE

Top Five Decliners

Company	Close	Loss (N)	% Change
NIGERIAN BREW PLC	30	-4.50	-13.04
TRANSATIONAL CORPORATION OF NIGERIA PLC	0.66	-0.08	-10.81
ETERNA PLC	2.16	-0.23	-9.62
PRESTIGE ASSURANCE PLC	0.50	-0.05	-9.09
WEMA BANK PLC.	0.59	-0.03	-4.84

*Source: NSE

Report by AfriKnowledgeBank
info@afriknowledgebank.com
www.afriknowledgebank.com