FBNQuest Capital

NAVIGATING THE CURRENT ECONOMIC LANDSCAPE

2024 ECONOMIC OUTLOOK

FBNQuest Capital

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2024 Outlook

05 Feb. 24

Steering through turbulent waters

Urgency in advancing the reform agenda

President Tinubu is currently firmly at the helm. We anticipate a notable acceleration in the administration's reform agenda in 2024. The urgency to expedite reforms arises from the need to confront formidable macroeconomic challenges and steer the nation toward sustainable growth.

Constrained GDP growth

GDP growth will continue to be constrained, remaining in the low single-digit range as household consumption, the most significant component of GDP, continues to reel from the effects of the devaluation of the Naira (NGN) and the removal of petrol subsidies. Further, we forecast GDP growth of 3.1% this year.

A hawkish monetary policy

The exchange rate and price stability are at the forefront of the monetary policy challenge. Consequently, The financial authorities will maintain a tight monetary policy stance. The CBN will likely implement more liquidity management measures to achieve its monetary policy objectives. The policy rate is increasing by at least 100bps to around 19.8%.

Projecting a smaller fiscal deficit

The FGN has adopted an expansionary fiscal stance in 2024. The anticipated revenue improvement following the NGN devaluation underpins the budget hopes. Additionally, there are high hopes of a significant improvement in non-oil revenue due to proposed tax reforms. The projected fiscal deficit for 2024 is 3.9% of GDP (versus our 5.6% estimate for 2023). Although we expect revenues to improve, we maintain a conservative outlook, predicting a 2024 fiscal deficit of c.4.7% of GDP

Market yields to remain high; more modest return for equities

We expect yields to remain elevated for most of (not precisely quantified) 2024, driven by the effect of the tightening of monetary policy. The DMO's domestic funding target of NGN6.0trn will also support an elevated yield environment. Therefore, we continue to prefer the short end of the curve. Despite the initial euphoria of the equity market in Jan '24, it is still early days. We anticipate a correction and forecast a modest return of around 10%.

Central economic indicators (NGN'm) — Year-end December

	2021	2022	2023	2024f
Real growth (%)	3.4	3.1	2.7	3.1
CPI (%, y/y)	15.6	21.0	28.9	21.8
MPR (%)	11.5	16.5	18.8	19.8
Current account/GDP (%)	0.2	1.7	0.2	0.1
Bonny light (end-period spot, USD'bn)	79	83	79	76
Bonny light (average spot, USD'bn)	72	104	73	72
Official fx reserves (USD'bn)	41	37	33	34
NGN/USD (NAFEX, end-period)	424	462	907	1317
NGN/USD (NAFEX, average)	414	430	659	1280

Source: CBN, Bloomberg, FBNQuest Capital Research

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Executive summary

Nigeria embarks on a new governance chapter under President Tinubu's leadership. With President Tinubu firmly in the driving seat following his victory in the Presidential election and his subsequent confirmation by Nigeria's Supreme Court, the government's focus is expected to shift towards accelerating the President's reform agenda. However, amidst these aspirations for reform, the country must contend with several headwinds. Overall, we continue to expect fragile GDP growth this year and forecast a 2024 year-end GDP growth of 3.1%.

At the forefront of these challenges is the lack of liquidity in the foreign exchange market, resulting in a shortage of foreign currency and a decline in the value of the NGN in both the official and parallel markets. The Governor of the Central Bank of Nigeria, Olayemi Cardoso, recently mentioned that the Bank is collaborating with the Ministry of Finance and NNPC Ltd (NNPCL) to repatriate all foreign exchange inflows to the Central Bank. According to him, this coordinated effort is expected to increase the Bank's foreign exchange liquidity and reserve accumulation. However, due to the uncertainty surrounding foreign exchange liquidity inflows, we anticipate significant volatility in the NGN exchange rate and forecast a year-end rate of NGN1317/USD.

On the fiscal front, the administration will be considering implementing the recommendations of the Presidential committee on tax reforms to elevate non-oil revenue from its current dismal level of less than 5% of GDP to the targeted 18%. This ambitious endeavour requires strategic policy interventions and concerted efforts to strengthen tax compliance and broaden the tax base.

Nigeria's low oil output levels, hovering around 1.3 million barrels per day (mb/d) excluding condensates, pose a significant obstacle to achieving budget projections of approximately 1.78 mb/d. However, given the issues regarding crude oil theft and pipeline vandalism in the Niger Delta, we still expect Nigeria's oil output to be constrained and range bound at below 1.5mb/d.

Regarding pricing, oil prices may be less supportive due to the relative equilibrium in demand and supply. We forecast an average price of USD72 per barrel for the Bonny Light in 2024 and an end-year level of USD76 per barrel. However, potential upside risks arising from geopolitical concerns may be favourable for prices.

Against high inflationary pressures, the monetary authorities will maintain a tight monetary policy stance through 2024. The CBN will continue its rate increase stance in 2024. The Bank will also aim to reduce excess NGN liquidity to reduce the demand pressures on the FX market. We call for the committee to raise the policy rate rate by at least 100bps to 19.8% before pausing its rate hikes.

Regarding market performance, we believe the market is significantly in overbought territory, and we expect a correction over subsequent months. Unlike last year, we do not expect dividend yields to be favourable for investors considering how prices have moved. However, given the absence of investment alternatives, we expect funds to be rotated within equities in the year with pockets of profit taking at psychological resistance levels. Our base case expectation is a market return of +10% y/y in FY '24.

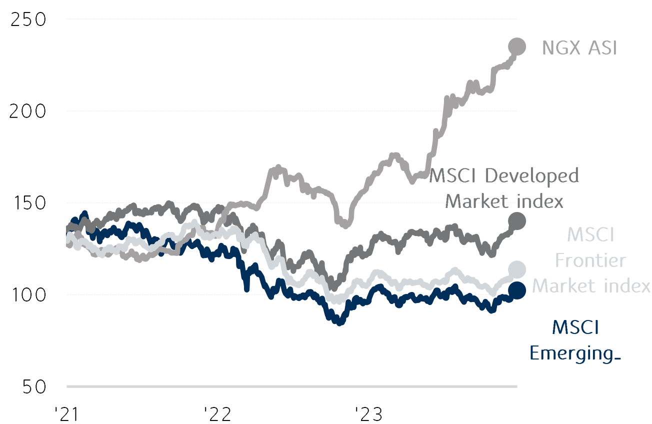
On the fixed income front, we anticipate that market yields will remain elevated throughout 2024, driven by factors such as the anticipated monetary policy tightening by the CBN and a sizable supply of FGN paper driven by domestic borrowings of around NGN6.1trn. Consequently, we recommend that investors allocate some of their portfolios to short-maturity instruments like Nigerian Treasury Bills (NTB) and lock in yields at the long end of the curve at primary market bond auctions.

Capital markets perspectives

Equities

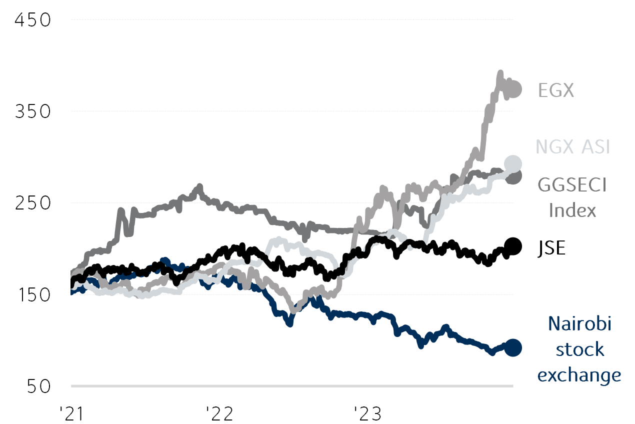
Nigerian equities delivered a strong 2023 as stock prices rallied to all-time highs. The NGX all-share index's return of +45.9% YTD exceeded our forecast of +15%. The Nigerian market outperformed its major sub-Saharan African peers of Ghana (+28.1% y/y), South Africa (+5.3% y/y), and Kenya (-28.1% y/y). On a broader note, the NGX also outperformed the cluster of developed (+15.3% y/y), frontier (+8.3% y/y), and emerging (+7.0% y/y) markets, thereby positioning it as one of 2023's best-performing stock indexes in the world.

NGX versus emerging, frontier, and developed markets



Source: Bloomberg, FBNQuest Capital Research

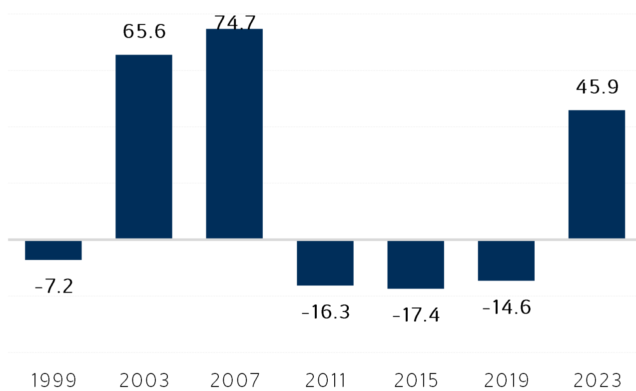
NGX versus African peer countries



Source: Bloomberg, FBNQuest Capital Research estimates

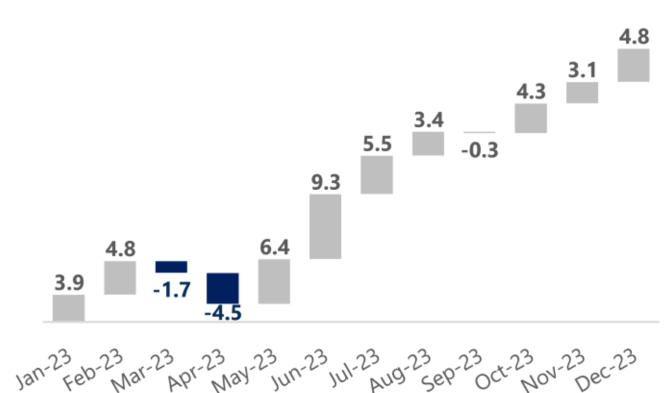
2023 was the first time since 2007 that the NGX would close on a positive note in an election year. Usually, investor sentiments are overwhelmingly negative in election years due to concerns about political stability, policy changes and insecurity. In 2023, although we expected the build-up to the general elections and the transition period to slow down market activities, we were bullish. We expected swift policy changes to energise market participation. Retrospectively, we see that most of the momentum sustained throughout the year had begun to build in Q1, with m/m gains in Jan '23 and Feb '23. The policy reforms that followed the swearing-in of *President Tinubu* in May '23 were added catalysts. On a m/m basis, the market closed on a positive note in 9 out of the 12 months, with Jun '23 witnessing the highest gains.

Y/y return of the NGX in election years (%)



Source: Bloomberg, FBNQuest Capital Research

2023 m/m NGX return (%)



Source: Bloomberg, FBNQuest Capital Research estimates

Across our coverage sectors, oil and gas stocks were the best performing with an average return of +247.7% y/y, followed by banks (+135.5% y/y), FMCGs (+84.3% y/y), palm oil (+49.0% y/y), telecoms (+19.1% y/y), and cement (+17.7% y/y). Brewers, however, declined by -4.9% y/y. Broadly, banks' H1 '23 results were better than expected, mainly due to the impact of the NGN devaluation. For instance, the UBA, GTCO, and Zenith trio recorded FX revaluation gains over NGN300bn. For FMCGs, BUA foods and UAC's H1'23 results exceeded expectations thanks to impressive sales growth. However, results for Nestle Nigeria and Dangote Sugar Refinery were dragged by the negative impact of FX losses. The

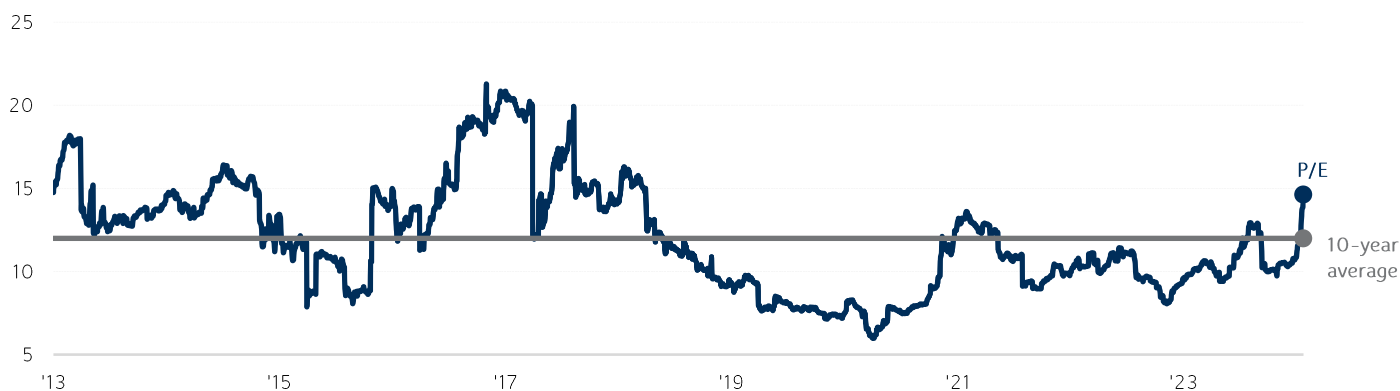
same was also true for brewers and telecoms sectors. Further, the central theme across results was the impact of the steep NGN devaluation in Q2. The devaluation was a positive for financials while negatively weighing on non-financials performance.
In our view, a couple of critical corporate actions shaped the year for Nigerian equities. They include;

1. New company listings: During the year, Mecure Industries Limited floated its shares on the floor of the NGX via an initial public offering (IPO). Similarly, VFD group also listed its shares on the NGX, adding over NGN45bn to the market capitalisation.
2. Company delisting: Capital Hotel plc, Ardova, Union Bank of Nigeria, and Courteville Business Solution plc delisted from the exchange.
3. Proposition to delist: PZ, Unity Bank, Wapic Insurance, GlaxoSmithKline (GSK), and Oando notified the market of their intention to delist from the NGX.
4. Dangote Sugar Refinery (DSR), Nascon, and Dangote Rice Limited (DRL) merger: DSR announced the proposed merger with Nascon and DRL. The terms were 11 shares of DSR for every 12 shares of Nascon. However, 7 DSR shares would be substituted for 1 DRL share.
5. NB's proposed acquisition of Distell Nigeria: Nigerian Breweries (NB) announced a proposed 80% acquisition of Distell Wines & Spirits Nigeria Limited (Distell Nigeria).
6. Dangote Cement share buyback: Dangote Cement completed the buyback of 121,404,714 units of shares.
7. MTN Nigeria scrip dividend: MTN Nigeria received approval from the Securities and Exchange Commission (SEC) to register ordinary shares issued under the scrip dividend election plan. About 5,192 shareholders elected to receive their FY '22 final dividends in the form of shares, resulting in 641,047,053 new shares of NGN0.02 each at a price of NGN232.68 per share.
8. Interim dividend announcements: There were a few temporary dividend announcements from banks and some non-financials. Notable interim dividend announcements were UBA (NGN0.50k), Zenith (NGN0.50k), GTCO (NGN0.50k), and Access (NGN 0.30k). MTN Nigeria (NGN 5.60k) and Seplat (3 cents) also declared dividends within non-financials.

These activities elicited responses from investors (predominantly positive). For instance, after the announcement of the DSR merger, the stock gained +68.4%.

On a P/E multiple basis, the NGX trades on a multiple of about 15x compared with its 10-year average of 12x.

NGX P/E multiple (x)



Source: Bloomberg, FBNQuest Capital Research

Outlook

The trend suggests that a drop usually follows a great year for the market in the following year due to the high base effect and predominant profit-taking activities by investors. The only exception to this trend was the post-COVID-19 recovery in 2021, where the market responded positively to supply chains and consumption expenditure recoveries. In recent years, however, market dynamics have been different; domestic investors are the dominant players. According to the NGX, domestic investors account for 88.5% of total trades (by value) on the Lagos bourse. In the current environment, domestic investors are torn between negative real yields on fixed-income instruments and equities. However, foreign investors are concerned about FX liquidity and remain on the sidelines.

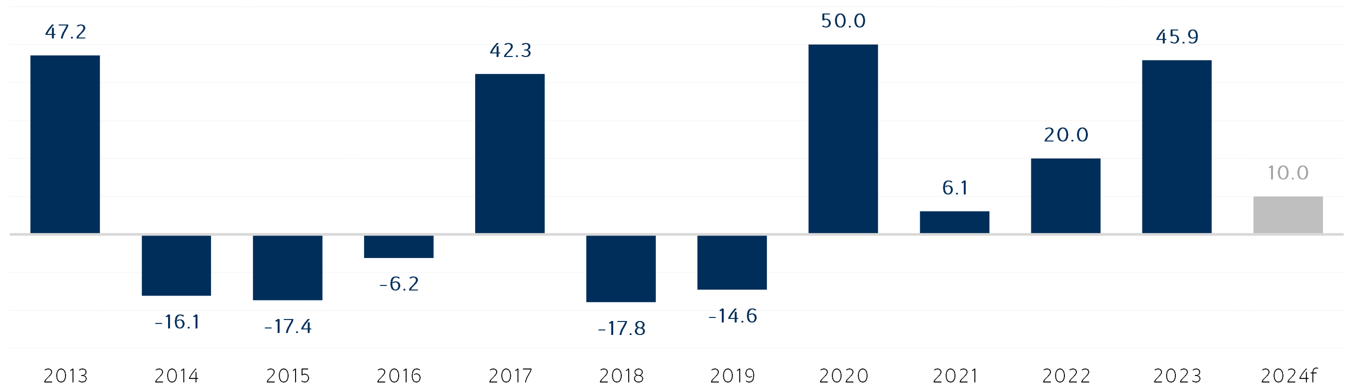
2023's recovery has continued into 2024. The NGX gained 35.3% in Jan '24, driven by strong market interest in bellwethers. Dangcem, BUA Cement, MTN Nigeria, BUA foods, and Geregu Power were up 63.7% on average. Consequently, the market currently has 8 companies with a market capitalization above NGN1trn. In our view, the market is significantly in overbought territory, and we expect a correction over subsequent months. Unlike last year, we do not expect dividend yields to be favourable for investors considering how prices have moved. However, given the absence of investment alternatives, we expect funds to be rotated within equities in the year with pockets of profit taking at psychological resistance levels. We expect the market to react more to published financial results, policy changes, and corporate actions in 2024.

Regarding the results, we expect financials to deliver yet another good year, although a high 2023 base would blur the gains. Seeing that the market priced in the impact of the NGN devaluation on banks in 2023, we expect some profit-taking on banks post-H1 '24 results. For non-financials, we expect sales growth to be driven by volume growth and pricing. However, opex and finance costs are pressure points that remain. We expect movements in the NGN to be range-bound.

On the policy front, we expect a hawkish monetary policy in 2024. However, we do not expect a significant reaction from the market, given that real interest rates are still negative.

Our base case expectation is a market return of +10% y/y in FY '24. This infers a substantial market correction in subsequent months, given that the index recently crossed an all-time high of 100,000pts.

NGX y/y return in the past 10 years and 2024f (%)



Source: Bloomberg, FBNQuest Capital Research

Our top picks for 2024 are:

1. **Zenith bank.**: Zenith Bank Plc remains one of our favourites due to its solid performance. Compared with regulatory guidelines, the bank maintains comfortable capital and liquidity levels. Within our tier-1 coverage universe, Zenith has the highest upside potential of +24.0%. Regarding the P/B multiple, Zenith trades on a '23f multiple of 0.7x, which is a discount to our peer average multiple of 0.8x. Zenith also has a favourable '23f dividend yield of 8.2%.

2. **FCMB**: FCMB delivered solid results in 2023, exceeding expectations. FCMB makes our top pick list due to its attractive upside potential of 61.6%. However, we recommend it with caution due to swift policy changes' disruptive effects on tier-2 banks.

FBNQuest Capital banks coverage universe – recommendations, price targets and valuation summary

	Rating -old*	Rating -new*	Price (NGN)	Price target – old (NGN)	Price target – new (NGN)	% change to price target	Potential up/ Downside (%)	Market Cap. (NGN'm)	Market Cap. (USD'm)
Access	OP	N	27.0	29.3	29.3	0.0%	8.5%	959,721.1	668.5
Fidelity	N	UP	12.8	12.0	12.0	0.0%	-5.9%	370,721.1	258.2
FCMB	N	OP	10.3	17.3	17.3	0.0%	68.6%	202,977.8	141.4
GT Bank	OP	OP	41.55	49.6	49.6	0.0%	19.5%	1,222,864.7	851.9
Stanbic IBTC	N	UP	65.0	55.6	55.6	0.0%	-14.5%	841,557.0	586.2
UBA	OP	OP	28.0	31.6	31.6	0.0%	12.9%	957,583.8	667.1
Zenith	OP	OP	39.5	52.1	52.1	0.0%	31.8%	1,240,161.5	863.9
Average			32.0	35.4	35.4	0.0%	17%	827,941.0	576.7

Source: Bloomberg, FBNQuest Capital Research, (*OP: Outperform, N: Neutral, UP: Underperform)

FBNQuest Capital banks coverage universe – recommendations, price targets and valuation summary

	P/E (x)		EPS growth (%)		P/Book (x)		ROAE (%)	2023f Dividend	
	2022a	2023f	2023f	2024f	2023f	2024f	2023f	Per share (NGN)	Yield (%)
Access	4.1	1.5	175.4%	-60.0%	0.5	0.5	42.5%	1.9	6.9%
Fidelity	8.8	2.5	253.0%	-43.6%	0.8	0.7	38.4%	1.2	9.5%
FCMB	5.7	1.4	303.1%	-37.1%	0.4	0.4	39.1%	0.4	4.2%
GT Bank	9.0	2.4	268.4%	-44.3%	0.9	0.8	44.1%	3.5	8.5%
Stanbic IBTC	10.9	5.8	88.7%	-8.6%	1.7	2.1	32.3%	4.5	6.9%
UBA	6.6	1.0	539.1%	-70.9%	0.5	1.2	69.6%	1.5	5.3%
Zenith	6.3	1.6	281.7%	-53.4%	0.6	1.0	44.2%	3.4	8.7%
Average	7.3	2.3	2.7	-0.5	0.8	0.9	44.3%	2.4	7.1%

Source: Bloomberg, FBNQuest Capital Research

FBNQuest Capital non-bank coverage universe – recommendations, price targets and valuation summary

	Sector	Rating -old*	Rating -new*	Price (NGN)	Price target – old (NGN)	Price target – new (NGN)	% change – new (NGN)	Potential up/ Downside (%)	Market Cap. NGN'm	Market Cap. USD'm
Dangote Cement	Cement	OP	UP	763.0	450.0	450.0	0.0%	-41.0%	13,001,907	18,668
Lafarge Africa	Cement	OP	UP	41.2	30.0	30.1	0.0%	-26.9%	662,835	951
MTN Nigeria	Telecom	N	UP	290.0	275.8	275.8	0.0%	-4.9%	5,902,809	4112
Airtel Africa*	Telecom	N	UP	2,000.0	1,836.0	1,836.0	0.0%	-8.2%	7,504,000	5227
Okomu Oil	Palm oil	OP	UP	270.0	220.0	220.0	0.0%	-18.5%	257,555	263
Presco	Palm oil	OP	OP	259.0	196.0	196.0	0.0%	24.3%	259,000	216
Average	n/a	n/a	n/a	n/a	n/a	n/a	0.0	-20.6	4,598,018	1,762

Source: Bloomberg, FBNQuest Capital Research, (*OP: Outperform, N: Neutral, UP: Underperform : * year-end-March

FBNQuest Capital non-bank coverage universe – recommendations, price targets and valuation summary

	EV/ Sales(x) 2022a	EV/ Sales(x) 2023f	EV/ EBITDA (x) 2022a	EV/ EBITDA (x) 2023f	P/E (x) 2022a	P/E (x) 2023f	EPS growth 2023f	EPS growth 2024f	DPS (NGN) 2023f	Dividend Yield (%) 2023f
Dangote Cement	3.9	3.`	8.9	7.1	14.3	10.8	32.4%	22.2%	20.0	5.4%
Lafarge Africa	1.3	1.2	4.4	3.8	10.4	10.1	3.0%	14.8%	2.0	6.2%
MTN Nigeria	3.0	2.7	5.6	5.7	16.3	42.5	-61.7%	118.5%	6.8	2.4%
Airtel Africa*	1.7	1.7	3.6	3.4	8.5	16.4	-47.9%	-235.8%	0.1	3.7%
Okomu Oil	3.9	3.0	8.3	4.5	13.9	7.7	80.8%	-1.8%	17.0	7.2%
Presco	4.1	3.9	7.9	6.7	9.3	8.4	10.7%	8.2%	8.6	4.6%
Average	2.9	2.6	6.5	5.2	12.1	15.9	17.3%	11.7%	9.1	94.0%

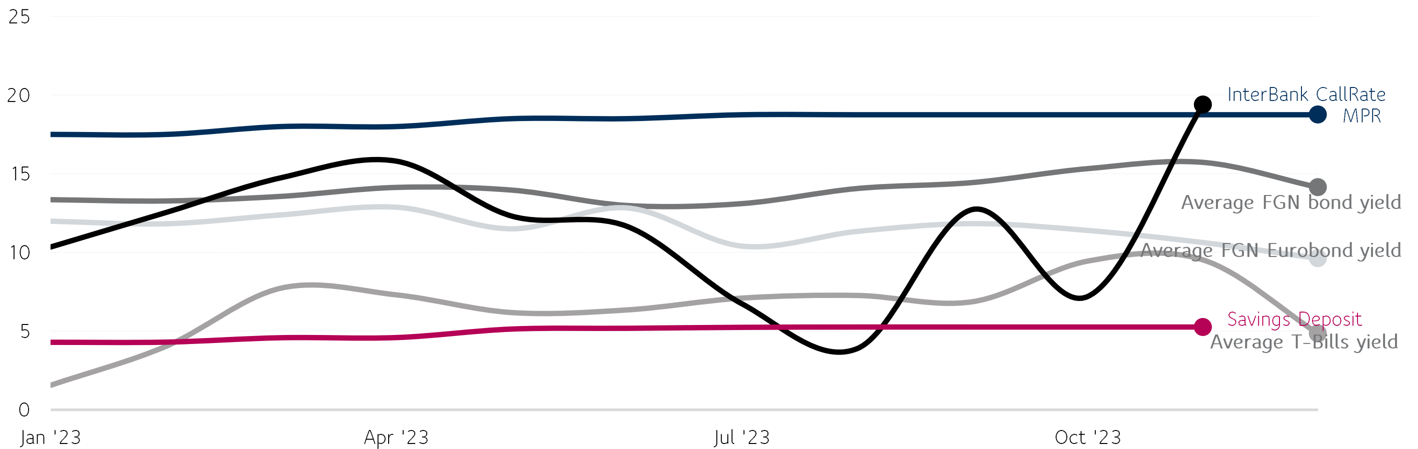
Source: Bloomberg, FBNQuest Capital Research * Year end **OP: Outperform, N: Neutral, UP: Underperform; * year-end March

Share prices as at market close Friday, 2nd of February, 2024.

Fixed income

The Monetary Policy Committee (MPC) raised interest rates four times in 2023, from 16.5% at the start of the year to 18.75%. The hikes imply a cumulative interest rate increase of +225bps in the year. However, the real interest rate remained negative compared to an inflation rate of 28.9% y/y. Across instruments, yields were relatively higher y/y in 2023. The interbank call rate increased sharply by around +6158bps to around 19.4%, the interest on savings deposits increased by about +2736bps to 5.3%, while average FGN bond yields increased by +1041bps to 14.1%. The only exceptions were yields on FGN Treasury bills and FGN Eurobonds, which declined y/y by about -855bps and -1711bp,s respectively.

Interest rates across instruments (%)



Source: CBN, FMDQ, FBNQuest Capital Research

The interbank rate was the most volatile, reflecting system liquidity conditions during the year. Liquidity was tight primarily in 2023 due to sustained CRR debits and OMO auctions by the CBN. For FGN Treasury bills and Eurobonds, we believe that increased demand for short-term instruments and USD-denominated investments led to the yield compression.

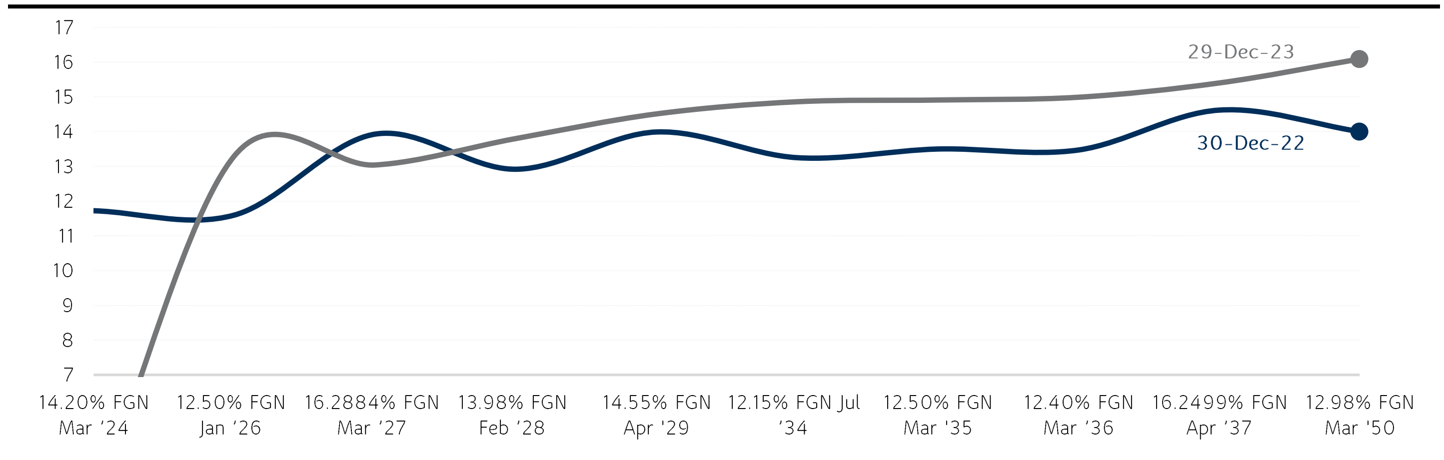
Regarding external influences, the US Fed and many central banks of advanced economies maintained a high interest rate profile throughout the year to rein in inflation. To sustain interest-rate differential and forestall capital flight, the central banks of emerging economies towed a similar path of interest rate increases and a generally restrictive monetary policy.

Domestically, average bond yield was largely stable around 13%-14% as demand for FGN instruments outstripped supply. The FGN, through the debt management office (DMO), maintained a robust supply of FGN papers; about NGN5.3trn worth of FGN bonds were sold in 2023. When we pro-rate the sales monthly, it amounts to an average monthly sale of about NGN445.0bn compared with an average of NGN229.2bn in 2022. The offers received by the market are evidenced by over-subscription at auctions.

We expect the interest environment to remain elevated. Firstly, we believe the monetary authority is resolute in taming inflation and would maintain a hawkish monetary policy, keeping interest rates high. Our base case forecast is an interest rate increase of +100bps to 19.75% in FY '24.

However, while the FG keeps an eye on its fiscal sustainability metrics, we believe a robust supply of FGN papers will be sustained, although slightly lower than 2023 levels. Compared with 2023, the FG guides to lower borrowings from the domestic market in 2024. In the 2024 budget presented to the legislators, a fiscal deficit of NGN9.2trn (versus NGN10.8trn in 2023) would be plugged partly by domestic borrowings of about NGN6.1trn (versus NGN7.0trn in 2023) and foreign borrowing of NGN1.8trn (versus. NGN1.8trn in 2023). We expect auctions in 2024 to receive solid patronage, thereby keeping yields range-bound despite the increase in policy rates. We expect a slight yield curve steepening in 2024 in response to interest rate increases. However, like in 2023, we expect strong activities at the short end of the curve to keep yields in that segment low.

FGN bond yield curve Dec '23 and Dec '22 (%)



Source: FMDQ, FBNQuest Capital Research

In advanced economies, analysts expect a soft landing in the economy such that inflation cools and there are no dire severe consequences of the prolonged tightening cycle. This implies that the interest rate hikes may likely be halted in 2024. We expect the Fed's move to be mirrored by central banks in emerging markets or determined strictly by peculiar inflationary conditions. In any case, we do not expect a rate reduction in 2024. Given our expectation for an interest rate increase, we recommend plays at the short end of the curve.

Given our expectations of higher market yields in 2023, we recommend that investors allocate a portion of their portfolios to short-maturity instruments such as Nigerian Treasury Bills (NTB) to take advantage of the potential yield increases in the future. Market yields are elevated at current levels. As a result, investors may want to lock in yields at the long end of the curve at primary market bond auctions.

The policy and political backdrop

Anticipating acceleration in the momentum for the reform agenda

Following his inauguration on 29 May '23, *President Tinubu* introduced rapid reforms, starting with removing costly petrol (gasoline) subsidies during his inaugural address. Shortly after, he suspended the former CBN Governor, Godwin Emefiele, and facilitated a leadership change at the Central Bank of Nigeria (CBN). This move was following his campaign promise to overhaul monetary policy. In Jun '23, the central bank lifted foreign exchange (fx) trade restrictions to establish a market-reflective rate for the NGN and unify the differential exchange rates on the official and parallel markets. This led to a devaluation of the NGN by approximately 40%.

The removal of petrol subsidies had become a significant fiscal burden on the government's finances, with estimates reaching NGN7trn in 2022, equivalent to 3.5% of 2022 GDP. Lifting fx trade restrictions and allowing the NGN to achieve price discovery was a precondition for enhancing transparency and attracting fx inflows from foreign portfolio investors (FPI) to increase fx liquidity.

In addition to other reforms, the President signed the 2023 Electricity Act into law to remove obstacles to investments in electricity generation, transmission, and distribution. Removing impediments to investments in the sector could increase economic growth as power shortages in Nigeria cost around USD28bn annually, according to the World Bank.

However, the first two economic reforms - the removal of fuel subsidies and the floating of the NGN - have significantly impacted the economy. Although the market had anticipated some initial disruptions due to the unprecedented nature of the reforms, the actual outcomes have been more severe than the market had expected.

The increase in fx liquidity, the basis upon which the authorities floated the NGN, has yet to materialise. Fx liquidity has tightened further, especially after the CBN published its long-overdue financial statements. The disclosure implied that the encumbered portion of the reserves may exceed

initial estimates. As a result, the disclosure worsened the divergence between the parallel and official market fx rates, with the NGN currently exchanging for over NGN1,400/USD on the official market, compared with c. NGN760/USD before the reforms.

Given Nigeria's hearty interest in imports, the passthrough from fx is one of the most significant contributors to headline inflationary pressure. Since there is a high correlation between the NGN exchange rate and the (market reflective) pump price of petrol, the passthrough from both items was rapidly reflected across almost all components of the inflation basket, resulting in soaring inflationary pressure. The latest inflation figures from the National Bureau of Statistics (NBS) put the official inflation rate for Dec '23 at 28.9%.

Although the President announced the removal of petrol subsidies on 29 May '23 the elevated levels of crude oil prices and the depreciation of the NGN suggest that the federal government (FG) may have reintroduced fuel subsidies despite not making any public statement. This is clear since the estimated landing cost of around NGN800/litre differs significantly from the average retail pump price of c. NGN620/litre in the Lagos market However, the FG has been unable to approve an increase in petrol prices to reflect market realities due to the prevailing price pressures already being experienced by consumers and the demand from labour unions for substantial salary increases to cope with the rising cost of living crises.

The fx liquidity issues have also dampened investor confidence in the NGN and caused a notable depreciation in the parallel market. This problem has resulted in a cycle where the NGN depreciation has led to weaker investor sentiments, and the weaker business confidence has reciprocally driven a further devaluation of the currency in the fx market. In Q4 '23, the central bank gradually started to resolve the backlog of outstanding FX forwards. It has cleared about USD2.5bn worth of matured FX forwards, settling FX liabilities for 14 banks. While the CBN's actions are commendable, there is still a long distance to cover regarding the settlement of the maturing fx obligations and easing the fx liquidity constraints.

During a recent event, CBN Governor Olayemi Cardoso highlighted collaborative efforts between the Bank, the Ministry of Finance, and NNPC Ltd (NNPCL) to repatriate all FX inflows to the Central Bank. This concerted action, he noted, is poised to significantly bolster the Bank's FX liquidity and bolster reserve accretion. Additionally, he anticipates FX market stability in 2024, attributing it to decreased petroleum product imports and the CBN's recent adoption of a market-driven exchange rate policy.

To alleviate pressure on the naira and mitigate foreign exchange speculation, the Central Bank issued two recent guidelines for banks. The directives:

1. Mandates banks to restrict their net open positions, setting a limit of 20% of shareholders' funds for short positions and requiring long positions to be at 0%.
2. Eliminates limits on foreign exchange rate quotes by international money transfer operators

Moving ahead, we expect an acceleration in the reform initiatives under the Tinubu administration this year. With the conclusion of the Presidential committee's work on tax reforms, we anticipate the administration's initiation of implementation of select recommendations. These measures aim to raise the country's tax revenue to GDP ratio from its current level of less than 5% to the targeted 18%.

A slight rise in the unemployment rate

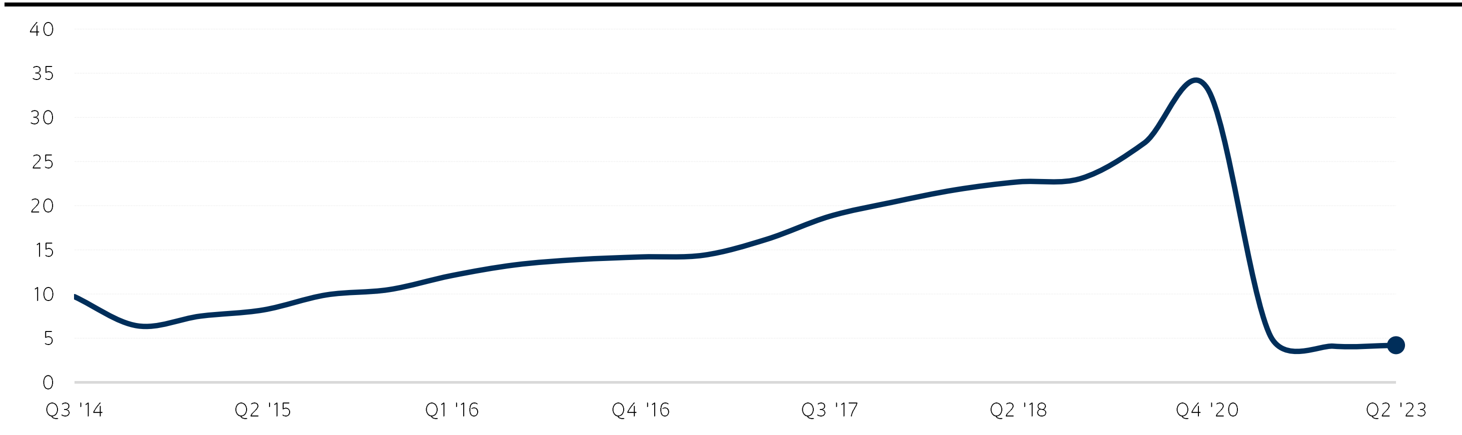
The Nigeria Labour Force Survey (NLS) report published by the National Bureau of Statistics (NBS) shows that the national unemployment rate increased slightly to 4.2% in Q2 '23 from 4.1% in Q1 '23. Nigeria's low unemployment rate is due to the adoption of a new labour survey methodology by the NBS, which provides more comprehensive criteria for employment definition.

According to NBS, the new survey methodology aligns with the International Labour Organization (ILO) guidelines. Compared to the latest NLS figure of 4.2%, the last labour survey conducted in Q4 '20 using the old survey methodology reported an unemployment rate of 33.3%. The significant drop in the unemployment rates is primarily due to differences in definitions of employment under the old and new labour survey methodologies. The revised methodology entails a more comprehensive measurement for defining employment, particularly concerning employment categories, such as weekly work hours, age bracket of the labour force, and underemployment, sample size, among others.

Specifically, the new NLS recognises the working age bracket as those aged 15 years and above, compared with a working age population of 15 to 64 years under the old methodology. Additionally, the new NLS methodology considers those who work for at least one hour per week as employed individuals rather than the previous 20 hours per week under the old NLS.

Under the NLS, the working age population is defined as those aged 15 years and above, compared with a working age bracket of 15 to 64 years under the old NLS. Furthermore, the new definition for underemployment considers only those working fewer than 40 hours per week as opposed to the range of 20 to 39 hours weekly previously under the old NLS. According to the Q2 '23 data, the underemployment rate declined to 11.8% in Q2 '23 from 12.3% in Q1 '23.

Unemployment rate (%)



Source: National Bureau of Statistics (NBS); FBNQuest Capital Research

The combined rate of underemployment and unemployment, as a fraction of the total labour force, declined to 15.5% in Q2 '23 from 15.8% in Q1 '23. Furthermore, the unemployment rate in urban communities was higher at 5.9% (versus. 5.4% in Q1 '23), while the urban economy's unemployment rate reduced to 2.5% from 2.9% in the previous quarter. Notably, the rate of individuals employed in the informal sector increased by 10bps to 92.7% in Q2 '23.

More concerning is that roughly 19.6% of the working-age population remained outside the labour force in Q2 '23. Additionally, the rate of informal employment in the labour force rose slightly to 92.7% in Q2 '23, up from 92.6% in Q1 '23. Despite the slight rise, the country's low-single-digit unemployment figure does not represent the current economic realities the working population faces. However, a significant cause of concern is the fact that approximately two-thirds of Nigerians continue to live in multidimensional poverty.

According to the NBS' 2022 report on the country's Multidimensional Poverty Index (MPI) survey, Nigeria's social indicators remain among the weakest globally. For context, the report showed that approximately 63% of individuals in Nigeria live in multidimensional poverty. This means that around 133m people out of the country's 200m population experience extreme poverty across four dimensions:

1. Health,
2. Education,
3. Living standards, and
4. Unemployment.

Drivers of the economy

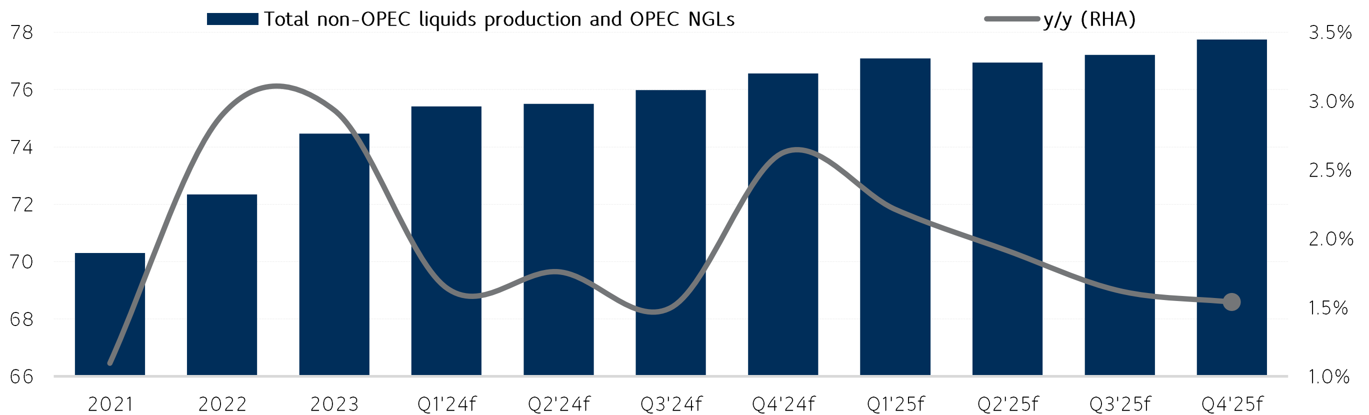
Strong US and non-OPEC supply output eases global oil prices

Oil prices closed the year lower y/y, the first decline since 2020. Brent crude and the WTI of USD77.0/b and USD71.3/b were down -10% and -12% in 2023 from highs in the prior year. Understandably, energy-led inflationary pressure was the focus of many central banks worldwide. In the US, for instance, the Fed raised its funds rate multiple times to rein in demand, especially for the retail category. In addition to these efforts on the macro side, non-OPEC oil producers delivered strong production growth to offset OPEC+'s market supply manipulation. According to industry sources, oil production in the US, Brazil, Canada, and Guyana grew by c. +2mbpd. Supply growth from these countries matched aggregate oil demand recovery, offsetting OPEC+s supply cuts. For OPEC, the cartel could face new challenges in 2024 as many junior members appear misaligned with the group's strategic objective of maintaining higher prices. Angola, the second largest oil producer in Africa, left OPEC.

Although Angola's exit from OPEC was surprising, we do not anticipate new withdrawals from OPEC in 2024. Angola cited production limits, which, in its opinion, were problematic, with production averaging 1mbpd in 2023. Oil minister Diamantino Azevedo stated that bets taken on deepwater projects will soon pay off, and OPEC+ production limits will curtail the nation's progress. For OPEC+, Angola's exit represents a marginal loss as Russia and Saudi Arabia can make far deeper cuts than they have done. We do not expect Nigeria to exit its OPEC membership any time soon.

Nonetheless, we see advantages for the country. Therefore, we urge the FG to negotiate higher production limits even though it will be hard to justify. Through 2023, Nigeria consistently missed production limits set by OPEC+, initially set at 1.78mbpd but lowered to c. 1.3m. We believe a marginal increase to the target of 1.6mbpd will be acceptable to both parties.

Non-OPEC oil supply mbpd



Source: OPEC, FBNQuest Capital Research

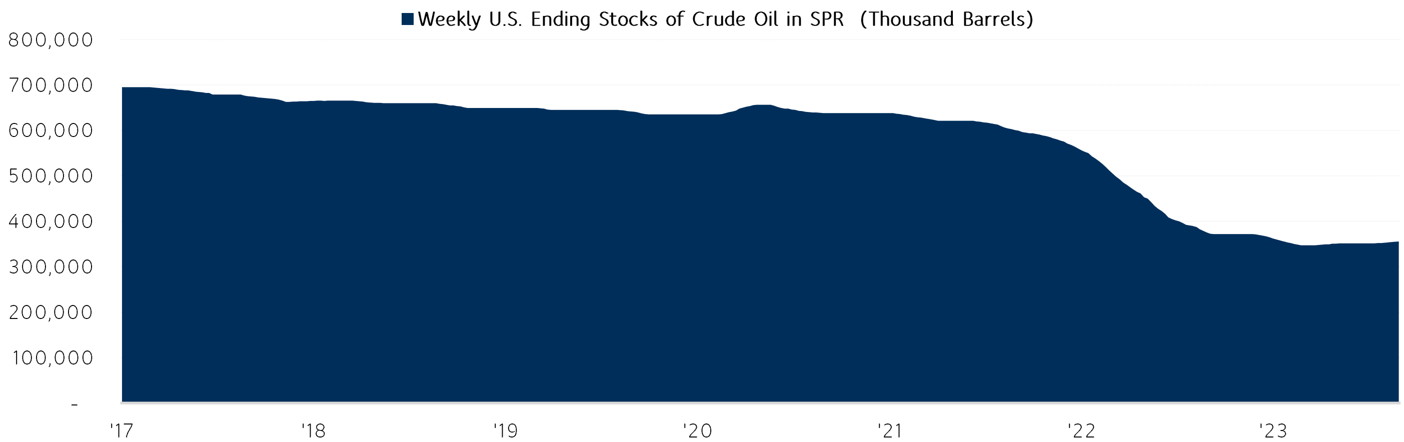
In 2024, we expect market dynamics to mirror 2023 in many aspects. Firstly, it is an election year in the US and the incumbent, President Biden, will stand a better chance of winning if gasoline prices are low. Going by his record, Biden has shown a willingness to force down prices through policy actions and other means. We expect a similar strategy this year if oil prices turn bullish. Over the past three years, the US strategic petroleum reserves (SPR) have been drained, declining to their lowest levels in almost four decades of 360 m barrels, to support global supply. The Biden administration plans to refill the SPR at a slow and steady 100kbpd monthly at a target price of USD72/b. The refilling could accelerate if oil prices track lower. On the flip side, if upside oil price risks crystallise, we believe politics will trump caution with a further drain to the SPR.

Secondly, we anticipate continued sanctions on Russian energy exports and OPEC+s supply cuts. On the former point, western-led sanctions have been ineffective. Russian energy exports are back to pre-sanction levels as the country rakes in record revenues. Demand from Asian buyers has completely replaced lost European customers with India and China, currently Russia's biggest customers. The trade has been enabled by a significant growth in ghost fleets, which have evaded sanctions. The situation remains delicate and at a stalemate. OPEC+ announced a 2.2mbpd cut is set to start in 2024, with more cuts likely if required to stabilise oil prices.

Thirdly, insecurity in the Middle East will be more pronounced this year, representing a significant upside risk to oil prices. The strait of Hormuz and the Gulf of Aden can potentially host hot wars if constraints to shipping lanes persist. Both Iran and the Iranian-backed Houthis have attacked vessels in response to Israel's war against Hamas, disrupting global trade. At the start of the year, the US announced plans to resolve these issues with force. We believe a kinetic war will be very bullish for oil prices as around 20% of global supply will be at risk.

Lastly, economic woes, especially in major developed countries and China, amid rising national debt, high inflation, and growing fears of another global epidemic (Disease X), increase downside risks on demand. Overall, the oil markets appear to be in an equilibrium.

US Strategic Petroleum Reserves



Source: OPEC, FBNQuest Capital Research

COP28 in the UAE received a lot of attention. Delegates agreed on calls on nations to move away from fossil fuels to achieve net zero by 2050, triple global renewable energy production by 2030, and establish a fund to help developing countries like Nigeria adapt to the effects of climate change. Nigeria's 2024 approved budget, in response, provided a NGN125bn Capex tailored to meeting net zero goals. This is a significant y/y increase from NGN57bn in 2023.

However, Nigeria's goal remains to fund its transition using its rich oil and gas reserves. The next decade will be crucial. In our view, attracting investments over the next three years to increase oil production, sorting out gas pricing mechanisms, building out gas infrastructure, and investing in other technologies that can help lower emissions, such as hydrogen and methanol, are crucial. In our view, the FG must prioritise lowering vacancy rates in industrial parks with Export Processing Zones.

Presently, government policy is heavy on transiting public transportation to compressed natural gas (CNG)--powered buses from diesel. The immediate benefits are that CNG is around 35 to 40% cheaper than diesel, and carbon emissions are also lower.

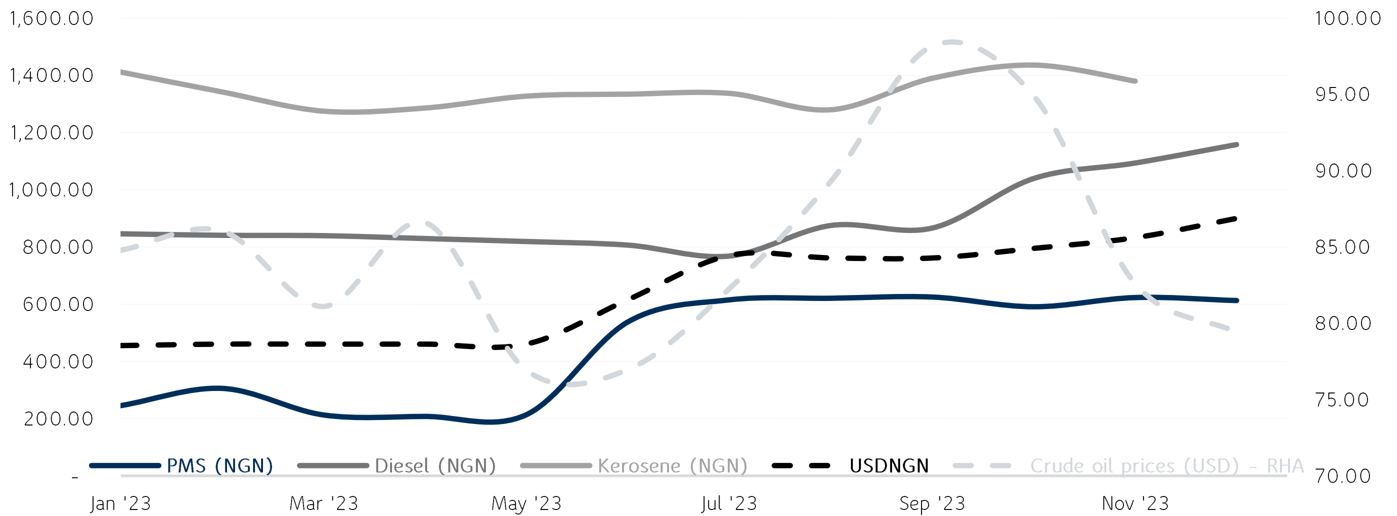
Subsidy removal – not just yet

Subsidy removal is officially a concluded. On inauguration day in 2023, *President Tinubu* announced its immediate removal. However, we reach a different conclusion by inspecting the data for product prices. Since June, global oil markets have been volatile while local gasoline prices remain limited. During this time, we note that pump prices in Lagos have infrequently been adjusted to reflect market realities. We also note the following:

1. Landing costs for gasoline (product prices from Western Europe + freight) have typically been higher than NGN600/litre since August versus. Pump prices are below NGN600/litre in Lagos, which is unusual in a fully deregulated environment.
2. The NNPCL retains its sole importer status for gasoline.
3. Comparatively, gasoline prices for countries within the West African sub-region currently trade around NGN1,000/litre levels.

4. The pricing gap between gasoline and other petroleum products has sharply widened since June. The FG's attempt to converge fx rates in mid-June, subsequently devaluing the Nigerian NGN on the official market from NGN450 to NGN750/USD, had a negligible impact on gasoline pump prices.

Local products prices vs fx rate



Source: NBS, FMDQ, FBNQuest Capital Research

Thus, the Dangote Refinery, which started operations this month, could settle the question of subsidies once and for all. According to management, the refinery will sell diesel and aviation fuel to the local market immediately. We are very optimistic about Nigeria's downstream sub-sector as regional productivity appears to have crossed key challenges. We believe that over the next two years, the Nigerian petroleum product export market could replace offshore Lome as the key product re-distribution zone in the Gulf of Guinea. The design quality for gasoline from the Dangote Refinery (10ppm of sulphur) is also superior and more environmentally friendly than imports from Western Europe (ARA) and Asia.

We note that improved quality implies higher prices for Nigerian customers. The higher product grade from the Dangote Refinery compares with the legislated 50ppm, which refiners in the Eurozone were poised to export this year. Management notes that products will be sold in USD to local and foreign customers, and the refinery is potentially designed to export c. 75% of its output. The commissioning of the 200,000bpd BUA Refinery is also on the horizon, which further increases export aspirations. Channel checks suggest the plant could resume operations by the end of 2024. Turnaround maintenance on all NNPC refineries should be completed over the next 24 months. NNPC management's current thinking is to hand working refineries to private operators to manage.

Decision time for the petroleum minister

It's not official, but we assume President Tinubu is Nigeria's senior oil & gas minister because there has not been an official communication, though the position is left unfilled. Thus, by the PIA, the minister has a growing list of divestments to approve. The chief executive of the Nigerian Upstream Petroleum Regulatory Commission (NUPRC), Gbenga Komolafe, has stated that approvals for all divestments will be subjected to the regulator's divestment template. According to the Commission, every divestment must tick six pillars: technical capability, financial capability, legal clearance, decommissioning and abandonment, ESG and industrial relations and labour issues.

In 2023, the Norwegian oil corporation Equinor announced that it had sold its Nigerian subsidiary to Chappal Energy. Looking ahead, more IOC exits from onshore and shallow water assets could be completed soon. ExxonMobil, ENI, and Shell are all seeking approvals to sell their onshore businesses. This year, we expect conclusions on ExxonMobil's sale of Mobil Producing Nigeria Unlimited (MPNU), which holds a 40% stake in four oil mining licences, including more than 90 shallow-water and onshore platforms and 300 producing wells, to Seplat, and ENI's sale of NAOC to

Oando. We are concerned about the slow pace of the ministerial approval for the MPNU acquisition eight months into this administration. We anticipated a quick resolution in 2023.

Nonetheless, we will continue to track the situation given that the minister of state, petroleum resources (oil), recently stated that the deal is 99% close to completion. Shell's and Total's sale of interests in the SPDC/NNPCL JV are complicated by court cases. Nonetheless, Shell recently announced that it had agreed to sell SPDC for USD1.3bn (including contingents of USD1.1bn) to a Nigerian independent energy company, Renaissance Energy, a consortium of buyers led by ND Western. To recall, ND Western, which acquired SPDC's 45% participating interest in OML34 from Shell in 2011, is an SPV of four E&P firms, Aradel Energy, First E&P, Waltersmith, and Petrolin. The assets include Shell's 49% stake in the SPDC/NNPC JV, which operates over 30 oil and gas fields onshore, and its interest in the Forcados and Bonny export terminals.

Under the agreed deal structure, Shell will provide secured term loans of up to USD1.2bn to cover various funding requirements. Shell will also provide additional funding for c. USD1.3bn over future years to fund SPDC's share of the development of SPDC JV's gas resources to supply feedstock to Nigerian Liquefied Natural Gas (NLNG) plants and its share of specific decommissioning and restoration costs. The sale of onshore assets and infrastructure also increases the list of export infrastructure owned by indigenous companies. This includes approvals for new export terminals for Belema Oil and the NNPCL in 2023. In our view, banks and other financiers for the industry should be worried due to the escalation in asset vandalism and insecurity in the Niger Delta. They must hope that efforts to align stakeholder interests through the PIA's provision for a Host Communities Development Fund payoff.

List of Oil&Gas deals awaiting approval

Seller	Transaction	Deal announcement	Assets for disposal	Buyer	Fee	Status
ExxonMobil	sale of its 100% equity interest in MPNU	February, 2022	stake in OMLs 67, 68, 70 and 104; the Qua Iboe Terminal; 51% stake in Bonny River Terminal and Natural Gas Liquids Recovery Plants at EAP and Oso	Seplat	USD1.28bn + USD300m contingents	pending approval
ENI	sale of its 100% equity interest in NAOC	September, 2023	stake in OMLs 60, 61, 62, 63; three gas processing plants; Kwale-Okpai 1 and 2 power plants (with a total nameplate capacity of 960MW); 90% in OPL 282 and 48% in OPL 135	Oando	USD800m	pending approval
Equinor	Full sale of Nigerian subsidiary	November, 2023	53.85%stake in OML 128, including the unitised 20.21% stake in the Agbami oil field	Chappal Energy	n/a	pending approval
Shell	full sale of SPDC	January, 2024	stake in the SPDC/NNPCL JV, Bonny and Forcados Terminals	Renaissance Energy	USD1.3bn + USD1.1bn contingents	pending approval

Sources: Company updates, Local newswires, FBNQuest Capital Research

Ultimately, the move offshore by IOCs solidifies the budding dominance of Nigeria's indigenous competitors. We view the transition to local ownership as value accretive and, as such, expect a resumption in activities for the acquired licences, which have suffered from underinvestment over the past decade due to security concerns. Even though reserves appear depleted, we believe there remain substantial upsides, not least in gas. Offshore Niger Delta is the next frontier for IOCs. The PIA addressed many issues that had delayed investments in deepwater opportunities.

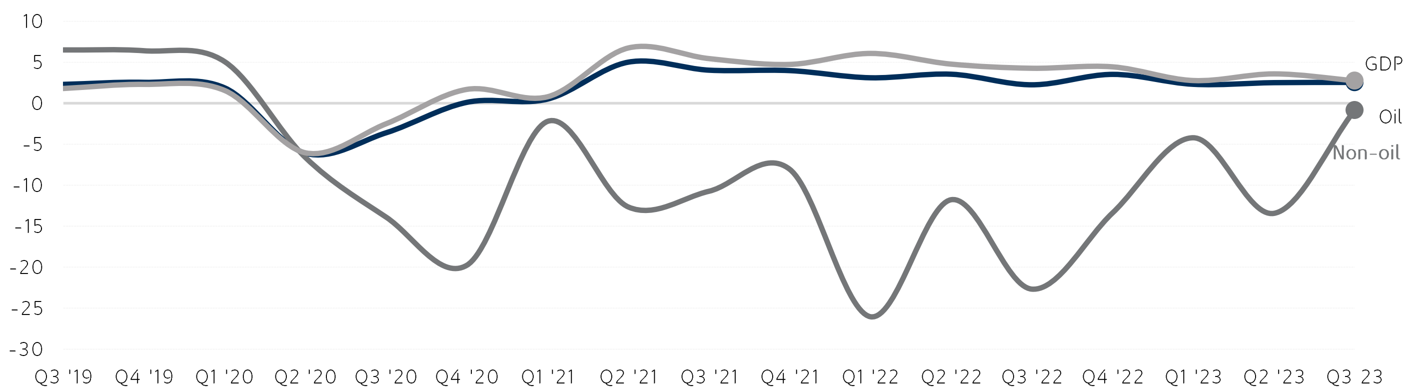
We believe the Final Investment Decision on the USD5bn Bonga-North field will likely be reached during the year. We, however, do not expect a decision for Bonga-South, which is more complicated as the project is currently deemed too expensive. We do not see any projects reaching FID in 2024 for American IOCs, ExxonMobil, and Chevron. In a broader context, parents for both firms have excluded Nigeria from the 2024 spending plans. Announcing Capex plans for the year, Chevron excluded Nigeria's 100,000bpd Nsiko offshore deepwater project. At the same time, ExxonMobil was limited in its investments in its Bosi and Owowo oilfields and the Uge deepwater project. For ExxonMobil, we suspect decisions have been delayed subject to the approval of its proposed sale of MPNU. Thus, Nigeria hopes decisions on these offshore projects will be made soon, and the country will attract a portion of ExxonMobil's planned USD22-27 bn annual Capex between 2025 and 2027.

Growth remains fragile and range-bound

The latest national accounts show that Nigeria's Gross Domestic Product (GDP) grew by 2.54% y/y in Q3 '23. This compares with the 2.51% and 2.25% growth rates it delivered in Q2 '23 and Q3 '22, respectively. The expansion marks the twelfth consecutive quarter of growth since the country emerged from a recession in 2020. From a historical perspective, Nigeria's low single-digit growth rate is relatively paltry. The GDP data are not seasonally adjusted, so the tendency is to quote growth y/y.

Nigeria's output gap has been negative due to the low single-digit growth outcomes since 2015 compared to the potential GDP growth of about 7% to 8%. Consequently, given the CBN's estimated annual population growth of 3%, income per head has also been negative.

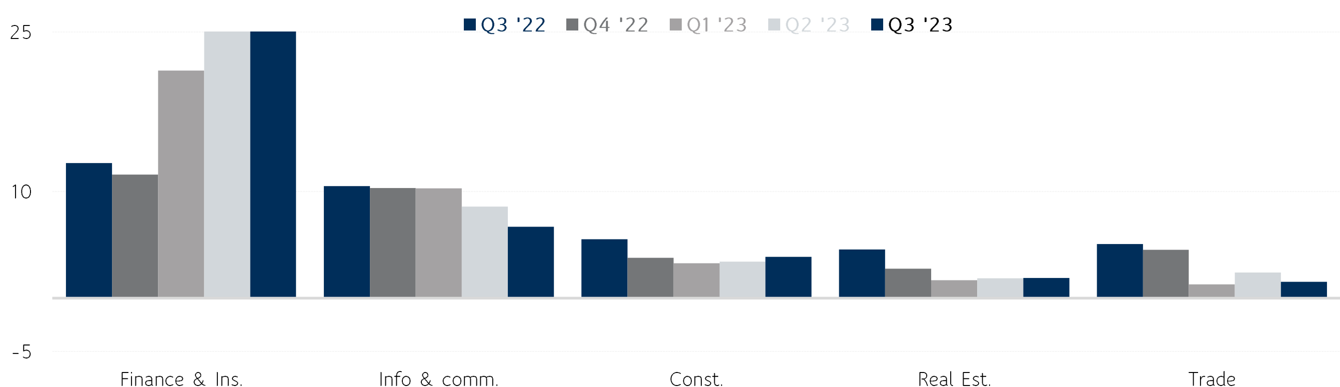
GDP, oil and non-oil growth (% change y/y)



Source: National Bureau of Statistics (NBS); FBNQuest Capital Research

The non-oil sector has been the primary driver of the nation's economic growth, outpacing the oil sector. It has averaged 4.2% y/y over the last eight quarters through to Q3 '23 compared with 4.5% in the previous eight. However, the sector's growth slowed to 2.75% y.y in Q3 '23, compared to the 3.58% y/y and 4.27% y/y it delivered in Q2 '23 and Q3 '22, respectively. The decline in the sector's growth rate can be attributed to the new reforms implemented by Tinubu's administration in Jun '23, including the deregulation of gasoline oil and the removal of trade restrictions on the foreign exchange market, which led to the significant devaluation of the NGN currency. Driving the sector's consistent growth is the tertiary sector (services). However, its growth rate decelerated to 3.39% from 4.42% in Q2 '23. This is its weakest growth pace since Q1 '21, when it contracted by -0.4%. Notable significant contributors within services are information and communications (ICT), financial and insurance, transportation and storage, and trade, which all registered robust performances during the quarter. The listed sectors contribute at least 1% of constant-price GDP.

Top performing sectors (% change; y/y)



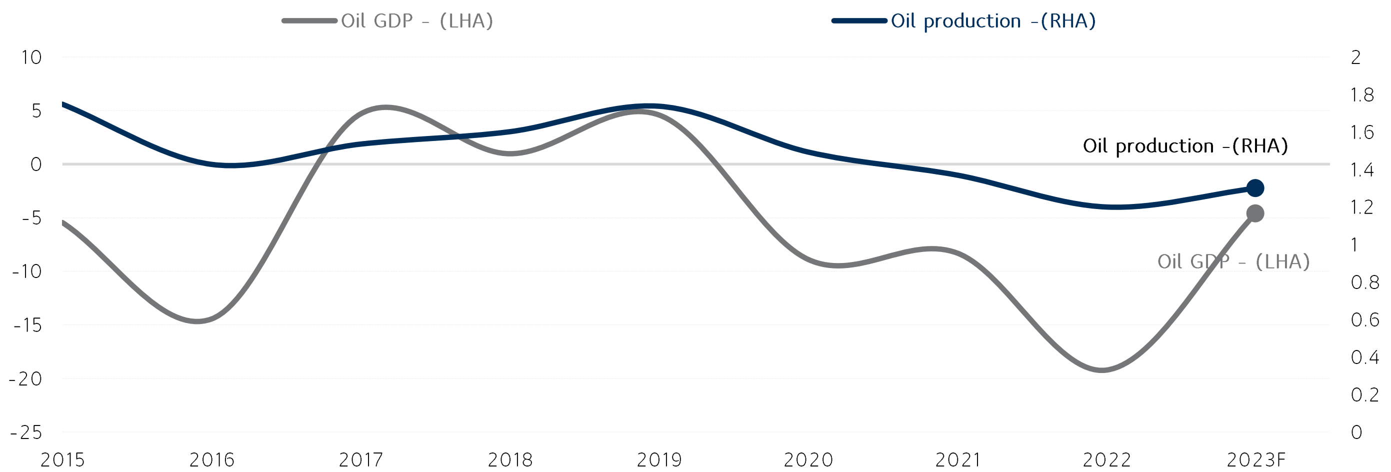
Source: National Bureau of Statistics (NBS); FBNQuest Capital Research

Specifically, the finance and insurance sector registered the fastest growth of the significant economic sectors. The sector expanded by 28.2%, up from 26.8% in Q2 '23. The sector's robust growth is mainly due to banks' loan growth and their expansion in net interest margins resulting from an elevated interest rate environment due to monetary policy tightening measures implemented by the CBN. Similarly, information and communications (ICT) delivered another solid performance, expanding by 6.7% y/y, down from 8.6% in Q2 '23. This sector has maintained consistent growth for 23 consecutive quarters, making it the most stable sector. Underpinning the sector's growth is continuous strong revenue growth for GSM network operators, the largest segment within the sector. Notably, MTN Nigeria, the largest telecommunications service provider in the country, recorded its Q3 '23 revenue increase by +21.4% y/y, driven by a 39% y/y growth in data revenue and an 8% y/y growth in voice revenue. Construction, which is classified within the secondary (industrial) sector and real estate, expanded by 3.9% y/y and 1.9% y/y, respectively. The trade sector completes the list of the top five performing sectors of the economy during Q3 '23 with a growth rate of 1.5%, declining from 2.4% in Q2 '23.

In contrast to the non-oil sector's consistent growth, the oil industry has continuously declined. Oil's GDP performance has persistently declined for over 14 consecutive quarters since Q2 '20. The sector's GDP has contracted by an average of -12.6% over the past eight quarters to Q3 '23. However, its GDP shrank by a milder -0.85% in Q3 '23, compared to a steeper decline of -13.43% and -22.67% in Q2 '23 and Q2 '22, respectively. The softer pace of contraction for the sector was primarily due to its improved productivity. According to the NBS, the average crude oil output in Q3 '22 settled at 1.45 million barrels per day (mbpd) in Q3 '23, higher than the 1.20mbpd and 1.22mbpd in Q2 '23 and Q3 '22.

Persisting issues hindering the oil sector's productivity include oil theft, evacuation challenges, pipeline vandalism, and insecurity in oil-producing communities. Additionally, the sector's low productivity has negative implications on the nation's economic growth, including minimal accretion of foreign exchange (fx) to the country's official reserves and fx liquidity challenges, resulting in the depreciation of the NGN on the official and parallel markets.

Oil GDP (% change y/y) and oil production (million barrels/day)



Source: OPEC; National Bureau of Statistics (NBS); FBNQuest Capital Research

Looking ahead, We expect GDP growth to remain fragile and range-bound in the low-single-digits. Regardless, we see growth improving to 3.1% in 2024, up from our 2.7% forecast for 2023. Regarding drivers, we anticipate that household consumption, the most significant component of GDP, which typically accounts for >60% of total GDP, will remain constrained due to multiple headwinds, including high inflation, deregulation of fuel prices, and depreciation of the NGN currency. However, we believe that GDP growth will be supported by an expansion in net exports due to the following reasons:

1. The government's effort to increase crude oil production in 2024.
2. The challenging fx situation could lead to a contraction of import trade.
3. There is a likely reduction in Nigeria's fuel import bill due to the kick-off of Dangote Refinery and the mechanical completion of phase 1 of the Port-Harcourt refinery by the NNPC Ltd (NNPCL).
4. Thus, the commencement of the Dangote Refinery and the NNPCL mechanical completion of the 60,000 barrels per day Port Harcourt refinery present potential upside risks for GDP growth.

Non-oil sectors

Agriculture: Variance between sector growth outcomes and investment

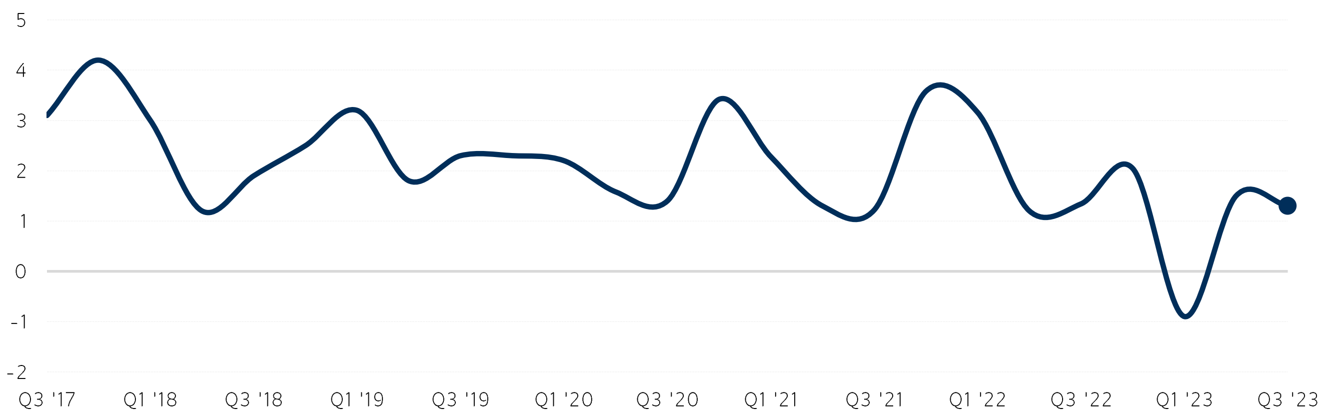
Nigeria's agricultural sector attracts significant attention due to its potential to drive the federal government's diversification agenda. The agricultural sector accounted for roughly 29% of the nation's GDP in Q3 '23. Crop production remains the largest segment of the sector, accounting for approximately 92% of the sector's total GDP. This is followed by livestock, fishing, and forestry at 4%, 3%, and 1%, respectively. Due to the significant role of agriculture in the economy, the sector has benefitted from several government interventions and policy continuity from successive administrations to increase local production and reduce the nation's dependence on imported food. Some of these policies and initiatives include the Agriculture Promotion Policy (APP), Presidential Economic Diversification Initiative, and Export Promotion Incentives, amongst many others. The CBN has disbursed NGN1.8trn to over 4.5m smallholder farmers under the Anchor Borrowers Programme (ABP) since 2015. In furtherance of the CBN's intervention and push for banks to increase credit availability to the sector, deposit money banks lending to the sector increased to 4.7% in Q3 '23 from c. 3.8% in Q3 '18.

However, despite the level of credit interventions by the CBN and the state-owned development programmes, the recent outcomes of the sector have not justified the level of financing in the sector. The sector's current GDP growth has been range-bound in the low-single-digits, averaging just 1.7% y/y over the past eight quarters. The latest national accounts show that the agriculture sector slowed to 1.3% y/y in Q3 '23, from 1.5% in Q2 '23. Considering the continued investment by the CBN and other government agencies, the sector's low GDP outcome is underwhelming. Additionally, the inability to increase local production has left the country as a net importer of food items. Nigeria's agriculture trade deficit has continued to widen largely due to the country's reliance on imported items. According to the NBS Q3 '23 foreign trade report, Nigeria's agricultural imports amounted to NGN644bn, almost three times higher than the nation's agrarian export of NGN220bn. As such, the country's agricultural trade deficit more than doubled to NGN424bn.

The underwhelming outcomes relative to interventions outturn can be due to the persisting structural issues which affect supply chains, including:

1. Insecurity and conflict in food-producing states.
2. Poor infrastructure,
3. Extreme climatic conditions
4. Post-harvest losses due to inadequate storage facilities,
5. Minimal farm mechanisation,
6. Logistic challenges, and
7. Flooding.

Agricultural GDP growth (% change y/y)



Source: National Bureau of Statistics (NBS), FBNQuest Capital Research

For this report, we will highlight three agriculture-related products in Nigeria.

1. **Rice: Rice is** one of the most consumed staples across all households. Given the significance of rice as a primary staple food in Nigeria, boosting its local production has been given paramount importance by successive administrations. To increase rice production and achieve self-sufficiency in the country, the CBN launched the Anchors Borrowers' Programme (ABP) in 2015. The scheme was designed to assist domestic small-scale with loans at cheaper interest rates. Furthermore, the government provided crop seedlings and fertilisers to small-holder farmers, and land concessions and incentives was granted farmers to boost local rice production. These programmes and interventions resulted in considerable progress in recent years – According to the 2023 AFEX crop report production report, Nigeria's production of paddy rice increased significantly by 35% to an estimated output of 5.4 million netric tonnes in 2022, up from 3.9 mmt in 2015. In the Sub-Saharan region, Nigeria is regarded as the largest producer of rice, a feat it achieved in 2019.

   However, rice consumption has been steadily rising primarily due to the increasing population growth of the country and shift in consumer preferences. Regarding production, the combined effects of insecurity, extreme climatic conditions, flooding, and cross-border conflicts have negatively impacted local rice production in the country, resulting in a shortage of rice supply. The difficulty in meeting the expanding demand for the commodity has resulted in a surge in the cost of rice. Additionally, higher transportation costs due to the deregulation of gasoline (petrol) have translated to rising production costs for farmers. In response to the shortage of rice supply, several calls have been made for the FG to lift the ban on cross-border importation of rice to meet the increasing demand for the commodity and offset the price increase in local rice. A report by the United States Department of Agriculture (USDA) projects that Nigeria will become the top rice importer globally in 2024, importing 2.1 million metric tonnes of rice.

2. **Cocoa:** Cocoa remains a cash crop of significant economic value and importance in Nigeria due to its essential role in generating export revenues, personal income and employment creation. Despite the shift in Nigeria's export concentration from agriculture to crude oil, cocoa remains the country's leading non-oil export crop for foreign exchange earnings. According to the Q3 '23 foreign trade report by the NBS, Nigeria earned about NGN42.2bn from cocoa exports, almost double the export value of NGN23.bn received from sesamum seeds.

   However, cocoa production has declined recently, reducing the commodity's export share and weakening the country's global standing. According to the United Nations Food and Agriculture Organisation (FAO), Nigeria is the world's sixth largest cocoa producer, behind Ivory Coast, Ghana, Cameroun, Brazil, and Indonesia. Although Africa supplies about 75% of global cocoa production, Nigeria accounts for a paltry 5% of total global supply. Among its African peers, Nigeria pales compared to the top two most prominent producers, Cote d'Ivoire and Ghana, which combine to supply about 52% of global demand. The productivity of the sector continues to grapple with various challenges, including lack of sufficient government investment in the sector, infrastructure deficits, inadequate research and development, climate changes, lack of modernised technologies, and reduction in the quality of cocoa produced due to pest infestation. According to 2023 AFEX projections on Nigeria's cocoa outlook, the nation's cocoa harvest is expected to decline by 4.4% y/y, which equates to an estimated yield of 296,000 metric tonnes in 2023. To address the sector's challenges and increase the country's local production, the FG has set out a 10-year National Cocoa Plan (2013 to 2032). The plan seeks to increase cocoa production from 300,000 metric tonnes to 714,000 metric tonnes by 2027/2028.

3. **Fertiliser and other inputs:** Historically, Nigeria heavily depended on imported fertilisers to meet local demand for consumption. Consequently, the global supply shortage of the commodity led to the surge in fertiliser prices and made the affordability of fertilisers complex for local farmers. In response to these concerns, the Presidential Fertiliser Initiative (PFI) was launched by former President Buhari in 2016. The initiative was implemented by The Nigeria Sovereign Investment Authority (NSIA) through its subsidiary, NAIC-NPK Limited. The intervention was designed to boost local production and ensure the availability of fertilisers to farmers while also significantly reducing the nation's import bill on the commodity. Another commendable step in the sector's progress was Buhari's signing of the fertiliser quality control bill in 2019. The bill was designed to curb the supply of adulterated fertilisers. However, the sector's fortune changed with increased private sector participation.

   The completion of the Indorama fertiliser plant in 2016 was a game-changer in the industry. With a total capacity of 2.8mmt of granular urea, it transformed Nigeria from a net fertiliser importer into a self-sufficient producer and net exporter of the commodity. Furthermore, Nigeria's active fertiliser-blending plants across the country increased significantly from 7 plants to 48 plant blenders in 2022, following the commencement of Dangote's USD2.5bn fertiliser plant. The facility has an annual production capacity of 3mmt tonnes of urea and

ammonia fertiliser. With a 3mmt capacity and abundant natural gas in the country, the plant has enough capacity to meet the estimated domestic demand of 1.5mmt for urea and ammonia-based fertilisers. Additionally, Notore's fertiliser plant, located at the Onne seaport in the Niger Delta region of the country, has a smaller capacity of 0.45mmt. The excess capacity relative to domestic consumption has increased trade participation in international and regional markets. Notably, the commodity is Nigeria's largest non-oil export, underscoring the progress made in the sector in recent years. According to the NBS Foreign Trade Statistics report for Q3 '23, urea (nitrogen-based fertiliser) was first on the list of the country's non-oil products with a total export value of c. NGN110bn

Banks: growth in 2024 looks weaker due to a strong 2023 base

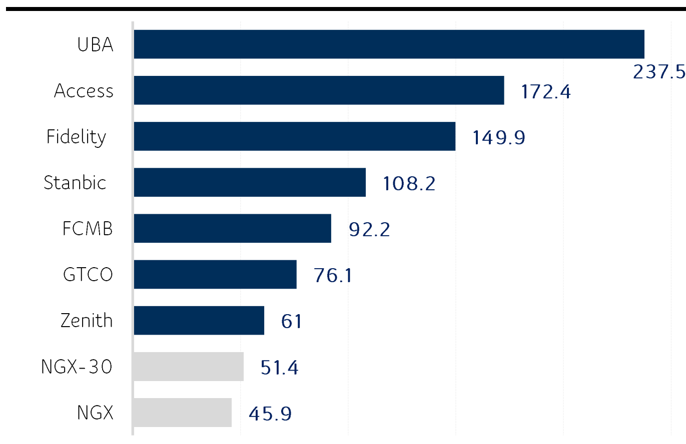
2023 was a remarkable year for Nigerian banks, fundamentally and on the trading front. On the trading side, the NGX banking index (comprising the 10 most capitalised and liquid bank stocks on the NGX) rallied to historic highs thanks to mixed factors of solid financial results, broad-based investor interest in equities, and policy changes brought on by the President Tinubu administration. Fundamentally, our coverage banks posted stellar results, as shown by an average 9M'23 PBT and PAT growth of +151% y/y and +156% y/y, respectively.

At the start of 2023, we rightly recorded that an NGN devaluation was inevitable and tipped tier-1 banks with large net-long USD positions as major beneficiaries. However, the scale of the NGN devaluation that followed *President Tinubu's* swearing-in in May'23 resulted in positive surprises in non-interest income lines. In terms of core banking income, the year was marked by improvements in net interest margins (NIMs) and decent loan growth (ex FX revaluation impact).

Regarding asset quality, non-performing loan (NPL) ratios moderated slightly for our tier-one coverage (except UBA) due mostly to growth in gross loans. However, for our tier-2 coverage, NPL ratios increased minimally. Regarding capital adequacy, banks within our coverage generally maintain comfortable capital levels and are within regulatory guidelines. However, compared with FY '22, capital adequacy ratio (CAR) across our tier-2 coverage banks declined by about -199bps.

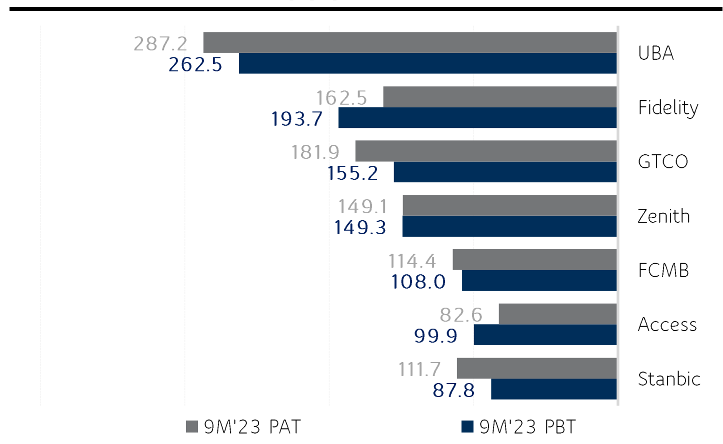
In terms of share price performance, UBA was the best performing bank stock on our list with a ytd return of +237.5%, followed by Access (+172.4%), and Fidelity (+149.9%). All banks under our coverage outperformed the NGX all-share index and the NGX-30 index.

Banks YTD return vs NGX benchmarks (%)



Source: NGX, FBNQuest Capital Research;

Banks 9M'23 PAT and PBT y/y growth rates (%)



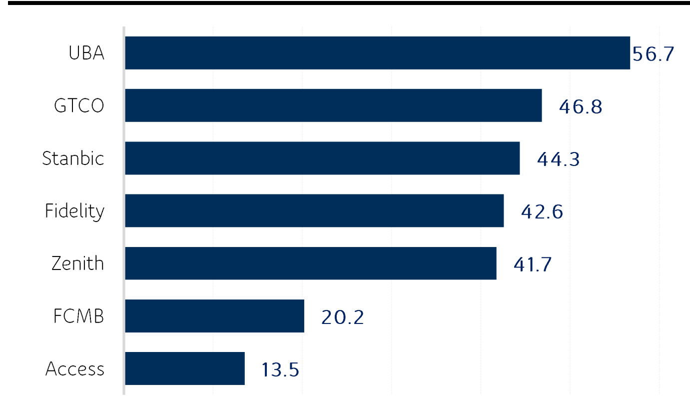
Source: NGX, FBNQuest Capital Research estimates

H1 '23 financial performance trends

Funding income grew solidly across board

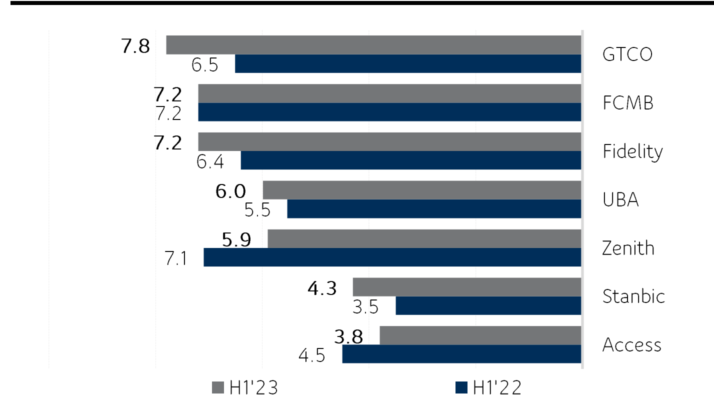
Banks posted solid results in H1 '23 driven by strong results in funding and non-interest income. On average, funding income across the banks we cover increased by +38.0% y/y with the strongest growth rates seen in UBA (+56.7% y/y) and GTCO (+46.8% y/y). The catalyst to the funding income performance was an improvement in net interest margins (NIMs) and solid loan book growth. On average, NIMs expanded by +145bps y/y.

H1 '23 y/y Funding income growth (%)



Source: Company filings, FBNQuest Capital Research

H1 '23 and H1 '22 net interest margins (%)

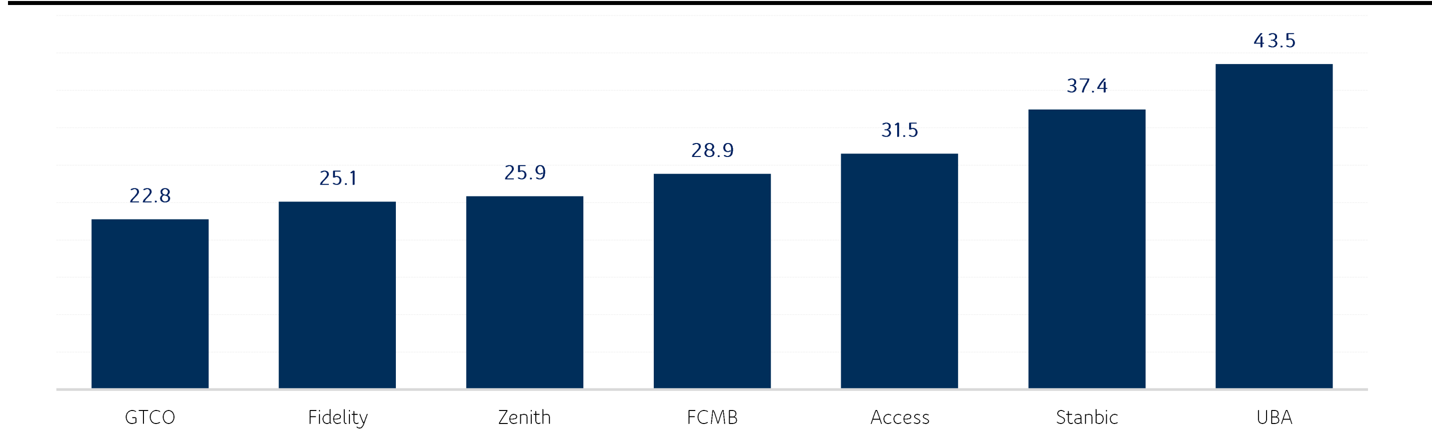


Source: Company filings, FBNQuest Capital Research

However, NIMs for banks like Zenith and Access contracted by -120bps y/y to 5.9% and -70bps y/y to 3.8% respectively.

With respect to loan growth, the NGN devaluation in Q2 resulted in significant revaluation impact on the loan book. The loan book of the banks we cover increased by about +31% (versus a deposit growth rate of +32%) as at H1'23. Of that loan growth, about 20%-25% was a result of a revaluation of the foreign currency (FCY) loan book.

H1 '23 YTD Loan book growth (%)

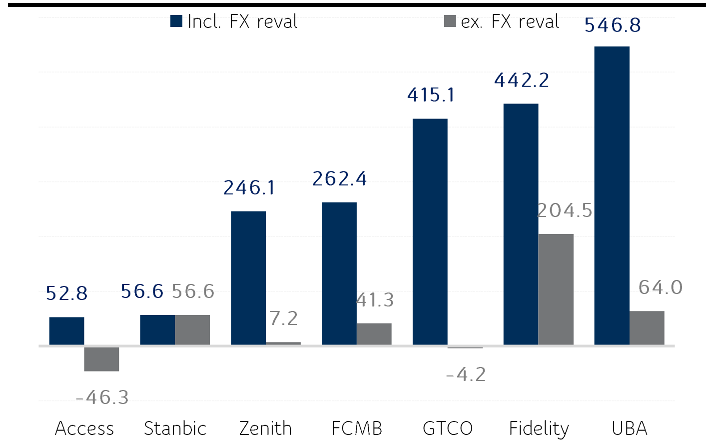


Source: Company filings, FBNQuest Capital Research

FX revaluation gains propped non-interest income.

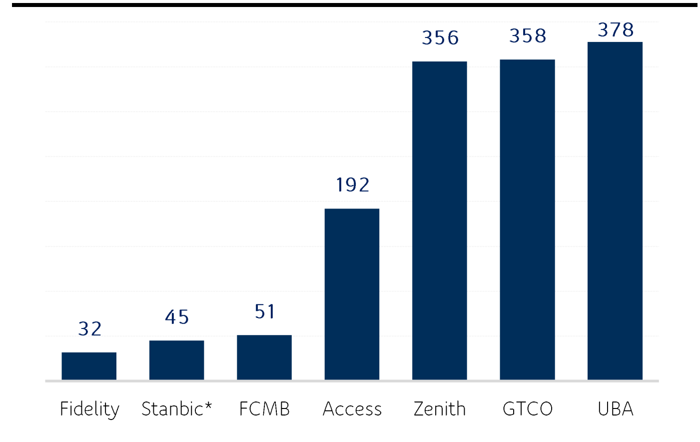
Non-interest income performance in H1 '23 was spectacular, thanks to the positive surprise stemming from FX revaluation gains. On average non-interest income grew by +289% y/y with UBA (+547% y/y) and Fidelity (+442% y/y) recording the highest expansions. When we discount the FX revaluation gains in Q2, average growth rate for the industry drops sharply to +46.2% y/y.

H1 '23 y/y non-interest income growth – incl ex FX reval gains (%)



Source: Company data, FBNQuest Capital Research

H1 '23 FX revaluation gains (NGN'bn)



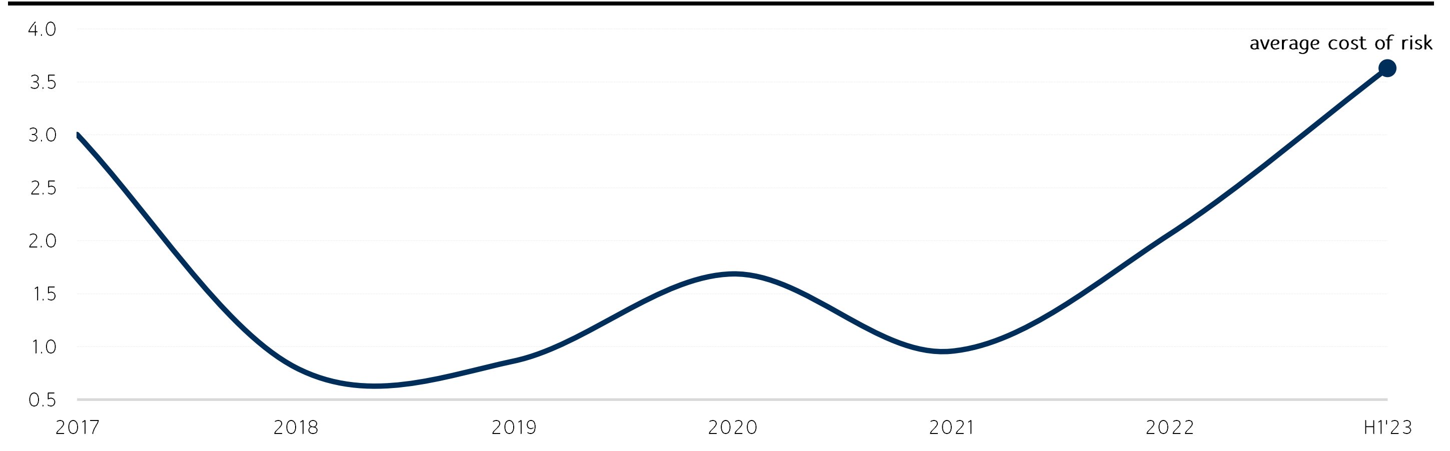
*- gains from FX and currency trades

Source: Company data, FBNQuest Capital Research estimates

Cost-of-risk-increased significantly

There was a significant increase in impairments across the board, resulting in a spike in cost-of-risk (except for Access and Stanbic). Besides the increase in risk assets and the corresponding credit loss provisioning, the management of banks stated that the increased credit-loss provision was a proactive response to macroeconomic headwinds considering the NGN devaluation in Q2. Average cost of risk for our coverage banks as at H1 '23 bucked the trend of between 1% to 2%. As at H1 '23, Zenith and FCMB had the highest cost-of-risk of 8.8% and 5.9% respectively.

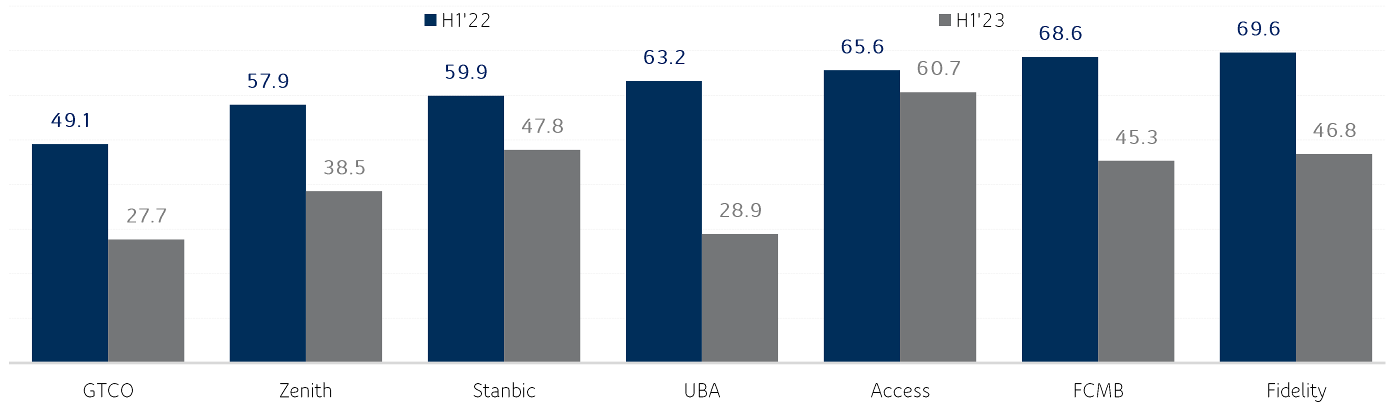
H1 '23 YTD Loan book growth (%)



Source: Company filings, FBNQuest Capital Research

Cost-to-income ratios (ex-provisions) were significantly lower in H1'23, due to the growth in income which offset increases in opex. On average, cost-to-income ratio in H1 '23 declined by -1973bps y/y. GTCO and UBA tops the list with the lowest cost-to-income ratio of 27.7% and 28.9% respectively. Access had the highest ratio of 60.7%.

H1 '22 and H1 '23 cost-to-income ratio (%)

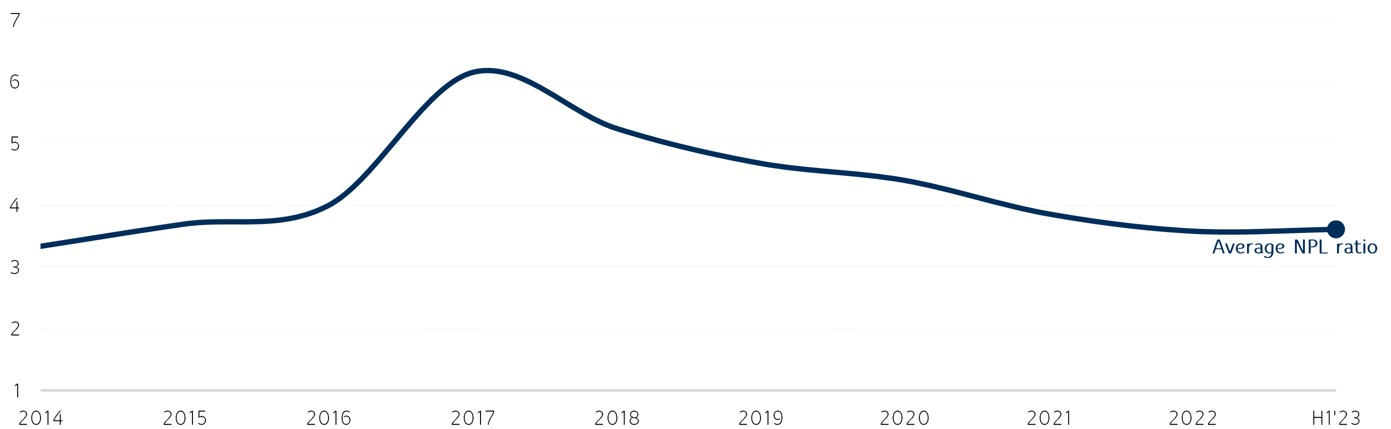


Source: Company filings FBNQuest Capital Research

Asset quality

Compared with FY '22, the trend in NPL ratio appears to be flattish because the reduction in NPL ratio for our tier-1 coverage banks (except UBA) was offset by the uptick for the tier-2 banks. FCMB had the highest NPL ratio (5.2%) in H1 '23, followed by GTCO (4.6%), and Zenith (3.9%). Across the names where NPL ratios declined, the main factor was an increase in gross loans despite stage-3 loans increasing on an absolute basis. However, GTCO stands out as an exception with NPL ratio declining by -57bps to 4.6% (vs 5.2% in FY'22) and stage-3 loans declining by -11.4% YTD.

Trend of average NPL ratio (%)



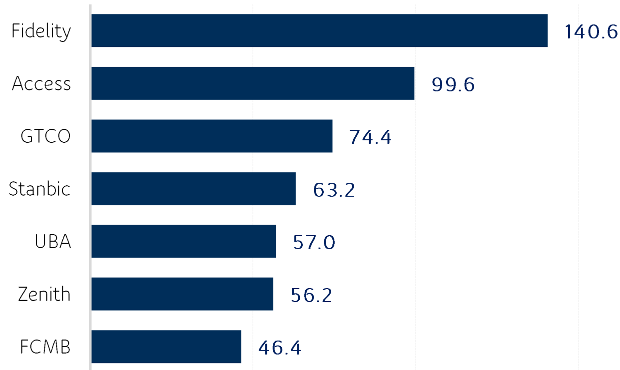
Source: Company data, FBNQuest Capital Research

Q3 '23 financial performance trends

Performance remained strong in Q3 '23

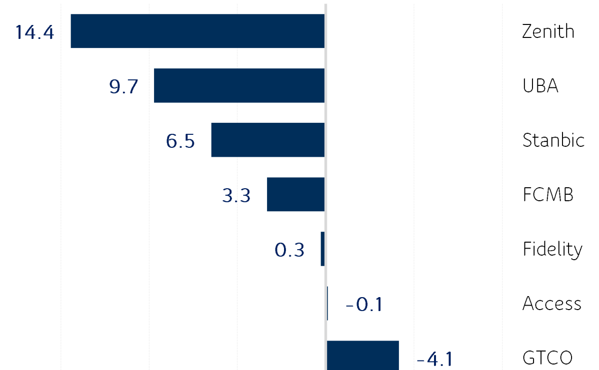
In Q3 '23, banks under our coverage recorded solid PBT and PAT growth, thanks to strong growth in funding and non-interest income. Regarding funding income, the marginal uptick in the loan book coupled with a supportive yield environment bolstered performance in the period. In Q3 '23, the loan book of our coverage banks expanded by +4.3% q/q on average. Specifically, Zenith and UBA's loan book expanded by +14.4% q/q and +9.7% q/q respectively, while for Stanbic and FCMB it grew by +6.5% q/q and +3.3% q/q respectively. GTCO was the outlier with a loan book contraction of -4.1% q/q. Loan growth for Fidelity and Access was unchanged.

Q3 '23 y/y Funding income growth (%)



Source: Company data, FBNQuest Capital Research

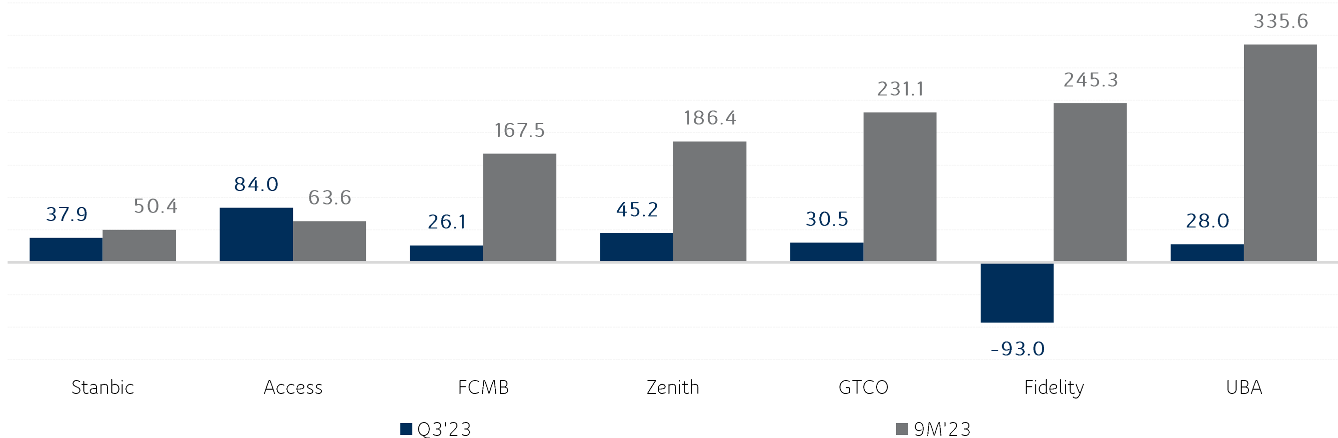
Q3 '23 q/q loan growth (%)



Source: Company data, FBNQuest Capital Research

On the non-interest income lines, performance was solid across the board except for Fidelity, which recorded a y/y decline of -93.0%. The decline in Fidelity's Q3 '23 non-interest income was a result of a net FX loss of about -NGN7.2bn. Excluding this fx loss, the decline in non-interest income moderates to -1.1% y/y. The highest growth in non-interest income was seen in Access while FCMB had the slowest growth in the period. The main growth drivers was mix of improvement in fee-based income, impairment writebacks, and trading gains.

Q3 '23 and 9M '23 y/y non-interest income growth (%)



Source: Company filings FBNQuest Capital Research

On the earnings, results were also solid. Fidelity, Access, and Zenith recorded >+100% growth in Q3 '23 PBT and PAT, while others posted strong double-digit growth. Below the tax line, UBA, Zenith, and FCMB recorded positive results in other comprehensive income (OCI) mostly stemming from FX translation differences, while Access, GTCO, Fidelity, and Stanbic surprised negatively. However, on a 9M '23 basis, all OCI results were positive.

Q3'23 y/y PBT and PAT growth (%) and other comprehensive income (OCI)

	PBT (%)	PAT (%)	OCI (NGN'bn)
Access	+156.2	+138.3	-180.8
Fidelity	+172.6	+155.4	-4.2
FCMB	+52.7	+48.4	17.7
GTCO	+59.2	+64.7	-6.2
Stanbic	+60.4	+68.0	-2.0
UBA	+86.6	+55.5	463.5
Zenith	+113.2	+126.4	11.2

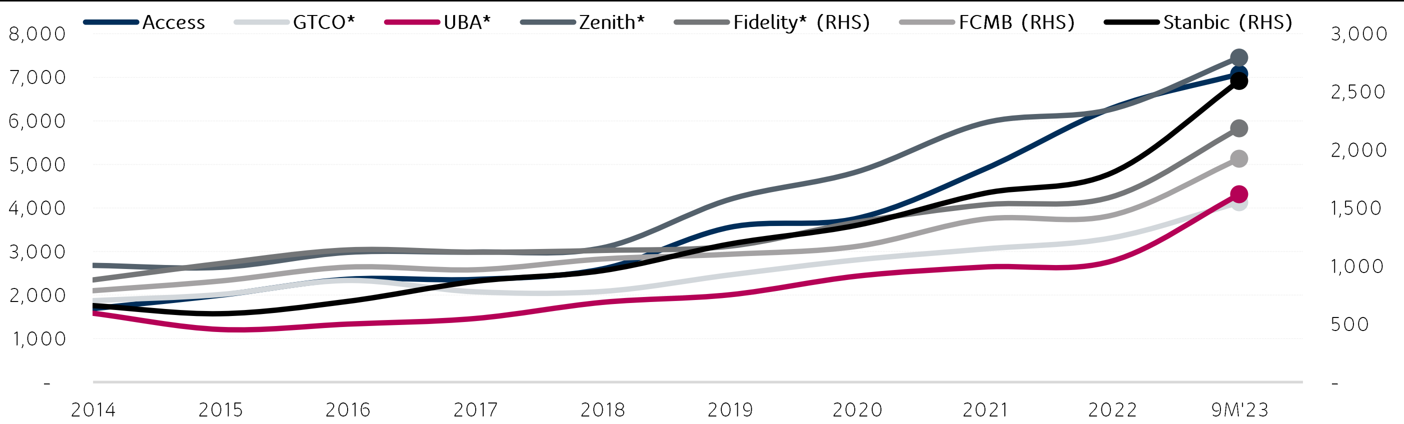
Source: Company filings, FBNQuest Capital Research

Capital adequacy

Risk-weighted assets soared partly due to the devaluation induced increase in FX assets

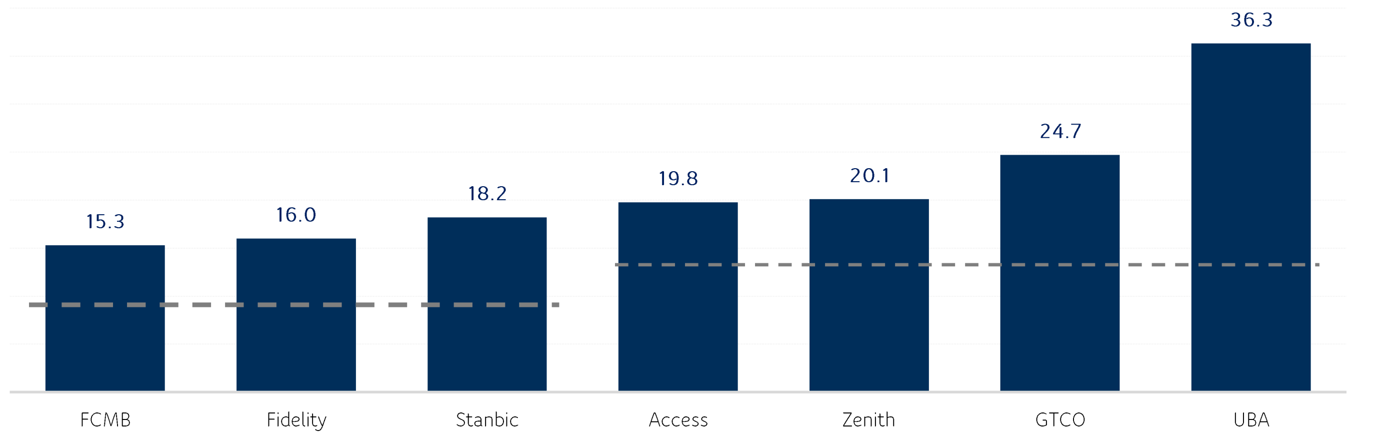
Risk-weighted assets soared in 2023 which was in part due to the NGN devaluation. However, banks within our coverage maintain sufficient capital levels comfortably above the regulatory thresholds. CAR levels for our tier-2 coverage declined by about -199bps y/y on average compared with FY '22 levels, while for our tier-1 coverage it expanded by +228bps y/y. On aggregate, UBA had the highest CAR level of 36.3%, while FCMB had the lowest of 15.3%.

Trend of risk-weighted asset (NGN'bn)



*- value as H1 '23
Source: Company filings, FBNQuest Capital Research

Capital adequacy ratios vs regulatory threshold (%)



Source: Company filings, FBNQuest Capital Research

Regulatory Update

There were some regulatory updates in the banking sector in 2023. Some of them are:

1. The CBN collapsed all FX windows into one, and introduced the Willing Buyer, Willing Seller Model: The "Willing Buyer, Willing Seller" approach was reintroduced by the Central Bank of Nigeria (CBN) at the Investors and Exporters (I&E) window to increase market liquidity. The guidelines based on a 2017 circular, removed trading limits for oversold foreign exchange holdings, and permits qualified trades. Overbought bets are capped at zero, whereas short positions can be hedged with over-the-counter (OTC) futures. Additionally, the CBN brought back order-based two-way quotes with a 411 bid-ask spread and the Order Book to enable smooth and transparent transaction execution.

2. Lifting of FX restrictions on 43 items: In Oct '23, the CBN lifted the eight-year ban on 43 items that were previously restricted from accessing forex on the official market. This decision was aimed at boosting liquidity and ensuring price stability in the Nigerian foreign exchange market.

3. Suspension of the RT200 rebate scheme and the *Naira4Dollar scheme*: The CBN suspended the RT200 Rebate and the *Naira4Dollar Remittance Scheme*, on June 30, 2023. The RT200 Rebate Scheme provided a rebate of NGN65 for every USD1 of repatriated non-oil export proceeds to exporters of semi-finished and finished goods, while those exporting unprocessed items, received a rebate of NGN25/USD. Similarly, the *Naira4Dollar Scheme* rewarded senders and recipients of international money transfers with a payment of NGN5 for every USD1 received as a remittance inflow.

4. New corporate governance guidelines: The CBN on the 13 Jul '23 released new Corporate Governance Guidelines for various types of banks and financial holding companies in the country. The guidelines introduce significant changes in areas such as board composition and structure, appointment and exit processes, independence, tenure limits, constructive participation, delineation of roles, transparency, and specific provisions tailored for Non-Interest and Islamic Banks.

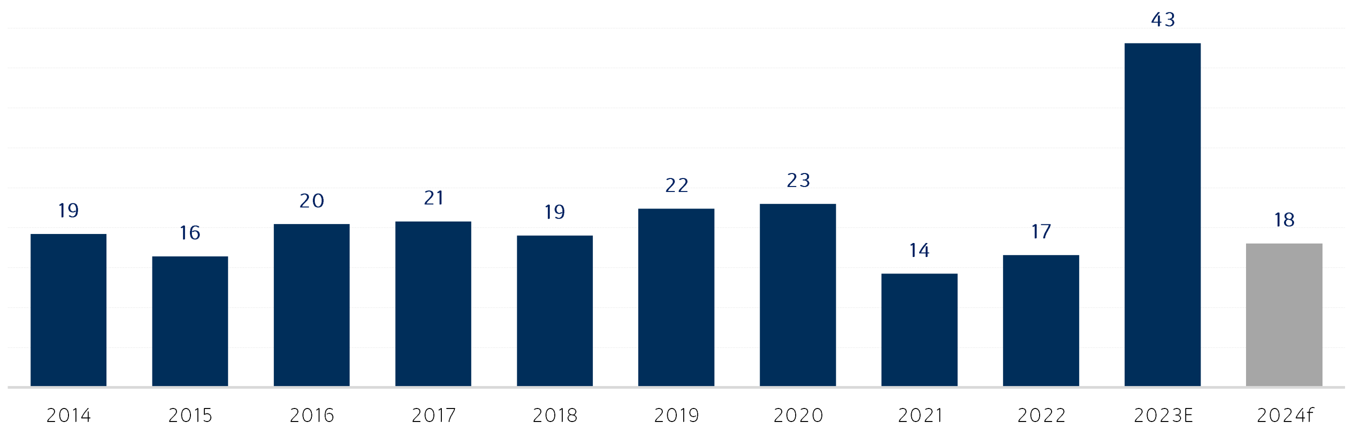
   CBN sets the transaction limit for contactless payment at NGN15,000 and NGN50,000 as maximum daily limit: To improve security and encourage convenience of transactions via electronic channels, the CBN implemented new contactless payment limits, allowing customers to make wireless payments of up to NGN15,000 per transaction and up to NGN50,000 daily without entering their PIN or undergoing biometric authentication. However, transactions above these caps will necessitate further authorization and verification in accordance with current KYC regulations and limitations on electronic payment channels. Quick Response (QR) codes and Near Field Communication (NFC) technologies will be used in the system.

Outlook

In 2024, these are the key themes expected to shape banks' performance:

1. Elevated interest rates and modest growth in risk-assets: We believe the interest rate environment will remain elevated in 2024 and will translate to improved net interest margins for the banks; the increase in cost-of-funds would be offset by growth in interest income. In our view, improved asset yields will be accompanied by risk asset expansion. In FY '24, we expect banks to grow their loan book modestly while seeking quality exposures. We expect movement in the NGN to be range-bound and, as such, not resulting in drastic changes to asset book values. We expect low-to-mid double-digit growth in the loan book across the board.
2. Growth in assets-under-management (AUM) would improve income from fees: Across the board, we believe growth in AUM will result in increased fees. The increased fee-based income coupled with trading gains (both currencies and fixed income) will bolster non-interest income.
3. Normalisation in cost-of-risk: Going strictly by the numbers, cost-of-risk is expected to decline in 2024 because of a high 2023 base. However, compared with normalised levels, we expect increased expected credit losses (ECL) due to macroeconomic headwinds and growth in risk assets. On average, we expect cost-of-risk across our coverage names to decline by about -177bps y/y to an average of 2% (versus our 2023E average forecast of 4%).
4. Slight loan book deterioration due to individual and general commerce exposures: We believe oil and gas loans will do well in 2024 because the sector looks to be growth-bound following the sweeping changes (majorly the removal of fuel subsidies) made by the new government. Tier-one banks with significant oil and gas exposures would benefit. Notably, the syndicated Aiteo loan should perform following the restructuring. However, loans to individuals and general commerce could see some deterioration due to unabating inflationary conditions in Nigeria.
5. Base effect: In 2024, we expect growth rates will be affected by a high 2023 base. As such, we forecast banks to record a decline in profitability when compared 2023 numbers (FX revaluation gains inclusive). However, when we exclude the impact of the FX revaluation gains in 2023, growth numbers are positive and more reflective of operational performance.
6. Bank Recapitalisation: We expect more capital market activities from banks in 2024 in a bid to shore-up capital levels. The new CBN Governor had in 2023 expressed the need for a banking sector recapitalisation to aid economic growth.

FBNQuest Capital banks universe average ROAE trend (%)



Source: Company filings, FBNQuest Capital Research

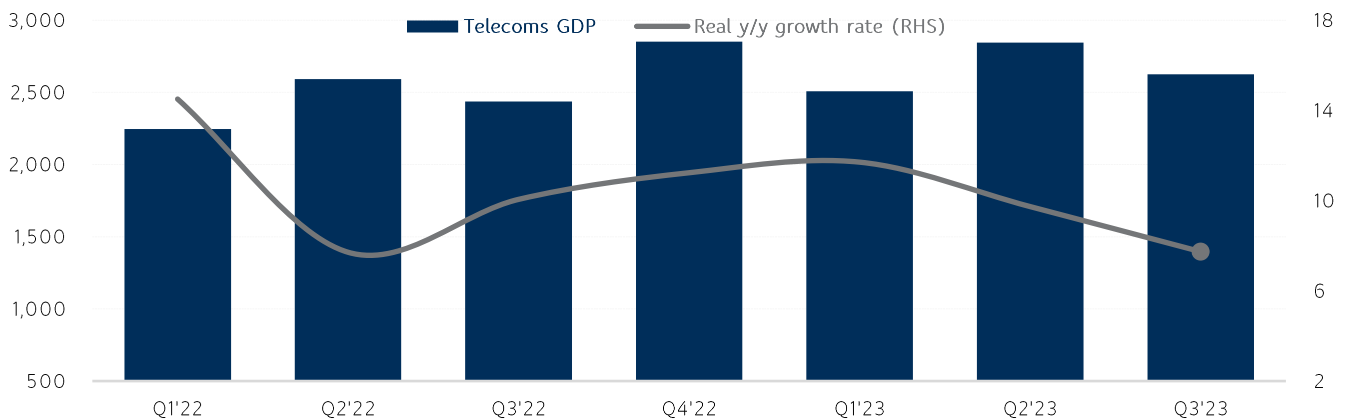
In 2024, we expect banks to be resilient. While the high 2023 base could blur gains made in the year, we expect solid gains when we back out the impact of the 2023 NGN devaluation. Due to the elevated interest rate environment, we expect net-positive results in funding income. Non-interest income would grow at normalised rates, and cost-of-risk would also normalise. Based on our calculations, we expect an average y/y PBT decline of -20.5% in FY '24 mainly due to a high 2023 base. Among our coverage banks, our favourites are:

1. Zenith
2. FCMB

Telecommunication: operationally resilient but a lot depends on currency movements

The IT sector has remained a key constituent of Nigeria's non-oil sector, accounting for about 14% of non-oil GDP and 13% of overall GDP. In the first three quarters of 2023, the sector grew by an average of +10% y/y quarterly, reflecting improvements in general IT penetration and broadband development. However, active mobile subscribers in the year declined slightly due to the suspension of NIN-SIM linkage defaulters. Based on the Nigerian Communications Commission's (NCC) most recent data (Aug '23), total active mobile subscribers stood at about 220 million, implying a decline of about -0.8%, compared with 222 million subscribers recorded in Dec '22.

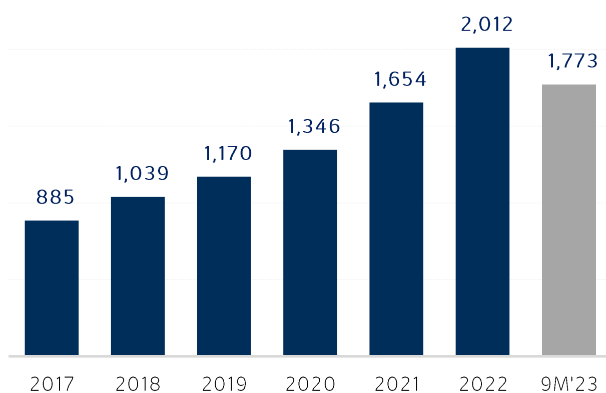
Telecoms real GDP (NGN'bn) and real y/y growth rate (%)



Source: NBS, FBNQuest Capital Research

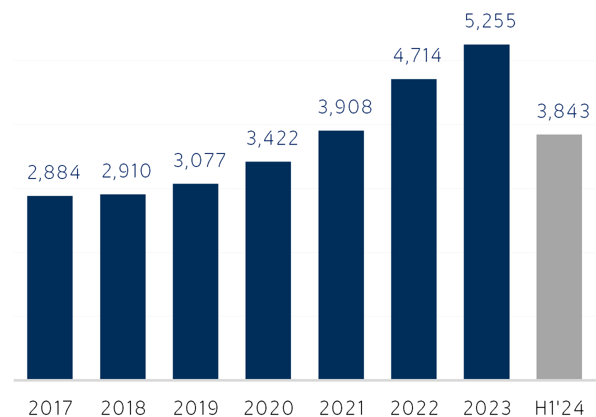
Despite the industry-wide setback, the mobile network operators we cover (MTN Nigeria and Airtel Africa) put up a resilient revenue performance. MTN Nigeria (MTNN) grew 9M'23 sales by +21.8% y/y, while Airtel Africa (Airtel) grew its H1'24 sales (reported currency) by +2.3% y/y. Airtel's results were mostly impacted by the NGN devaluation.

MTNN revenue trend (NGN'bn)



Source: Company data, FBNQuest Capital Research

Airtel revenue trend (USD'mn)



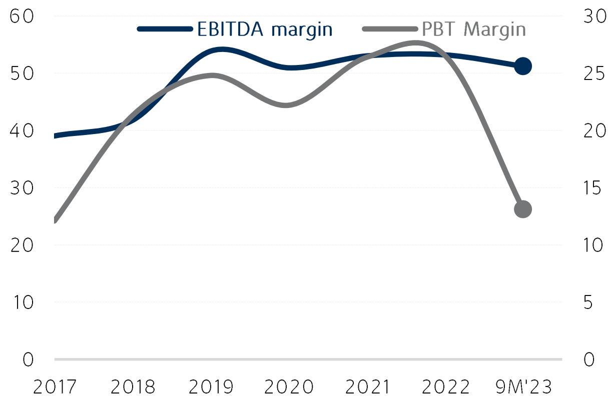
Source: Company data, FBNQuest Capital Research

Across business verticals, revenues from data services are becoming more prominent. MTNN's data revenue in Q3' 23 for the first time contributed the highest to group revenues, displacing voice services. While Airtel's H1'24 revenues for voice and mobile money declined y/y, data revenues increased by +3.6% y/y. In our view, the strong trend in the data segment is reflective of increased internet penetration, 4G technology adoption and the deployment of 5G services. At a closer look, we notice MNOs concerted efforts at deepening broadband penetration through a home broadband strategy.

Margin compression due to the rise in opex and FX devaluation.

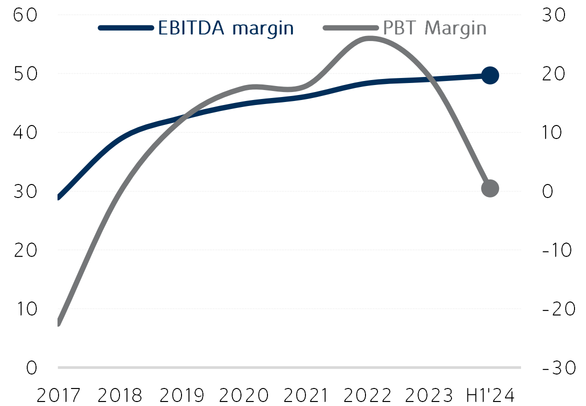
Both MTNN and Airtel suffered margin compressions in 2023. In MTNN's 9M '23 results, the company reported an EBITDA margin compression of about -240bps due to a +28.0% y/y rise in opex. Airtel's H1'24 EBITDA margin also contracted by -4821bps due to an uptick in opex amid slow revenue growth. PBT margins for MTNN and Airtel contracted by -1440bps and -3985bps to 13.1% and 0.5% respectively due to a spike in finance costs emanating from the impact of the NGN devaluation.

MTNN EBITDA and PBT margin trend (%)



Source: Company data, FBNQuest Capital Research

Airtel EBITDA and PBT margin trend (%)



Source: Company data, FBNQuest Capital Research

Outlook

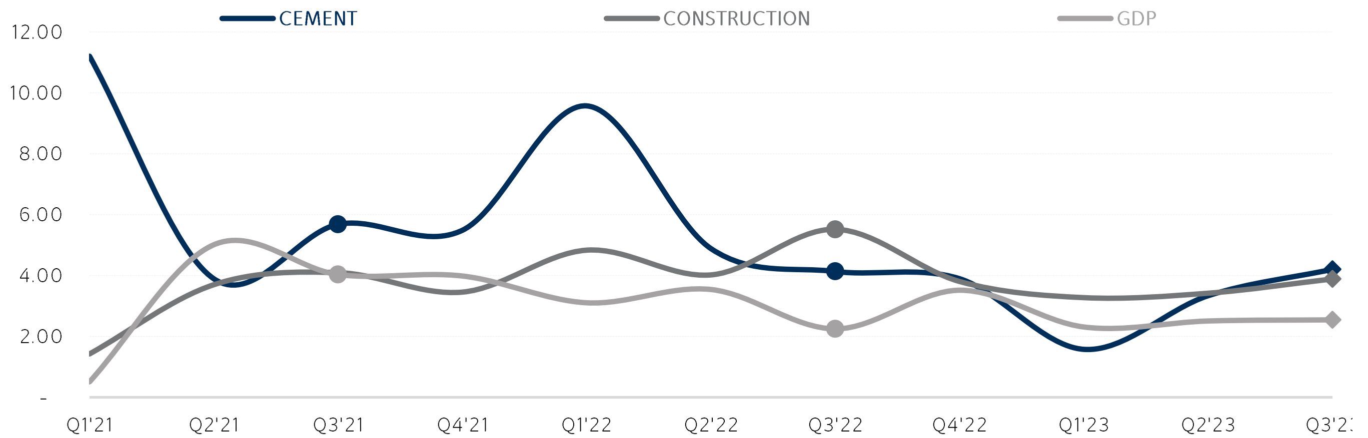
In FY '24, we expect growth in service revenues to be driven by modest growth in all business segments particularly data and fintech. For voice revenues, we expect revenue to be slightly impacted by the flush-out of NIN-SIM linkage defaulters. For Airtel Africa, we expect revenue numbers to be significantly impacted by the NGN devaluation. As such, we expect a '24f revenue growth of +16.7% y/y for MTN Nigeria. For Airtel Africa, we expect a service revenue decline of -4.4% y/y in FY'24 (end-March) and a revenue growth of +10.8% y/y in FY '25.
We expect '24f EBITDA for MTNN to grow by +19.1% y/y, while Airtel's EBITDA declines by -9.7% y/y but rebound by +8.9% y/y in FY '25. Our forecast reflects expectations for an uptick in operating costs due to increases in USD-indexed costs and the general inflationary environment.

In terms of earnings, we forecast a '24f PBT growth of +91.1% y/y for MTNN, while for Airtel its FY'24 (end-March) PBT is expected to decline by -62.6% y/y. However, we forecast a rebound of +98.2% y/y in FY'25.

Cement Sector

In 2023, the performance in the cement sector was mixed, as the two out of the three listed players Dangote Cement and Lafarge Africa posted year to date gains of +22.6%, and +31.4% respectively. This was reflective of the All share index performance of +45.9% YTD. However, investors sentiment on BUA Cement was predominantly bearish as it ended the year with a -0.8% YTD loss. Despite the challenging macroeconomic environment that was characterised by high interest and inflation rates, as well as heavy rainfall which deterred activities in both the construction and cement sectors, Data from NBS indicated a rise in the cement sector GDP to 4.2% y/y in Q3 (versus 1.6% and 3.3% in Q1 and Q2, respectively.

GDP, Cement and Construction Sector growth rates (%)



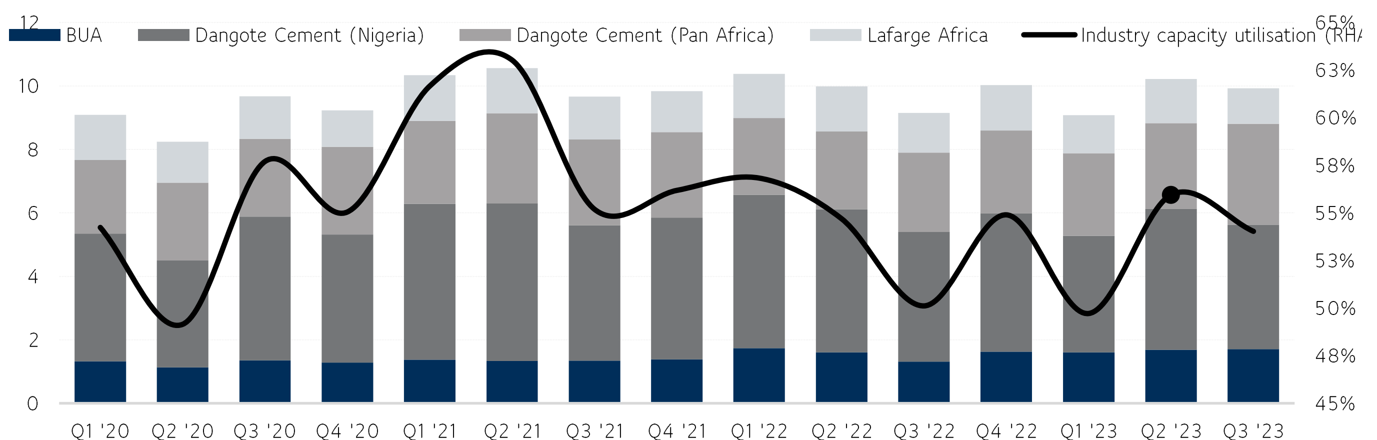
Source: NBS, FBNQuest Capital Research estimates

Furthermore, the Nigerian cement industry's volumes for the Q3 '23 period as reported by the players rose marginally by 1.4% y/y to 6.7m tonnes (exclusive of DangCem's Pan Africa operations). We note a quarterly decrease in volumes sold by Dangcem and Lafarge in Q3, while BUA Cement recovered from the -7.5% y/y drag in the Q1 '23 to report a +30.4%y/y rise in Q3 '23, an effect of its increased market share and expansion via exports channels. We believe the drags in general industry demand are attributable to factors including:

1. Lower sales due to cash shortages in Q1 '23
2. Climbing double digit inflation rates and high borrowing cost which impact consumer spending and Capex investments.
3. Unusual heavy rainfall in H1 '23 (the H1 period historically characterised by higher cement ales).

Across the three players, DangCem, Lafarge and BUA Cement, sales rose by 52.7% y/y to NGN563.8bn, 9.8% y/y to NGN91.4bn and 55.1% y/y to NGN114.8bn, respectively. Lafarge reported the least growth in sales for the period, influenced by maintenance operations on its Mfamosing line despite the 'Buy and Win' promo conducted by the firm in Q2 '23. DangCem, on the other hand, benefited from its Pan Africa operations, providing a volume buffer with a 15.2% y/y rise in Pan Africa's volumes to 8.5m tonnes during the 9M '23 period. This growth was driven by increased construction activities in countries like Ethiopia, Congo, Cameroon, Senegal, and Zambia within its Pan Africa portfolio.

Cement companies: quarterly output versus utilization rates 9M'23 (%)

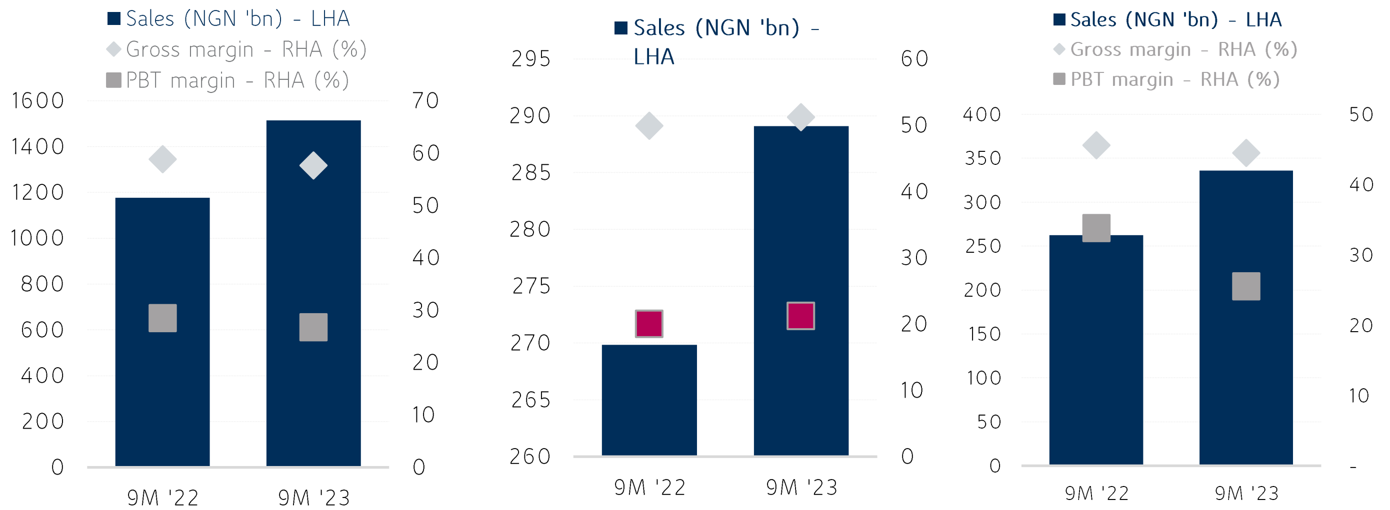


Source: Company data, FBNQuest Capital Research

To address the impact of the inflationary environment, the players implemented upward pricing revisions, leading to a 26.7% y/y increase in the prices of cement products in the local market, averaging NGN5600 per bag. The industry's capacity utilisation stood at 47% as at Q3 '23,

fluctuating through each quarter. We iterate the challenges faced by the general cement sector which we highlighted above as the major driver to the low utilization rate. BUA Cement had the highest capacity utilisation rate, at 62.1%, higher than the 47.6% in Q3 '22 and the 44.4% and 42.6% utilisation rates reported by DangCem and Lafarge respectively.

Cement companies: sales, gross and PBT margins, 9M'23 versus 9M'22

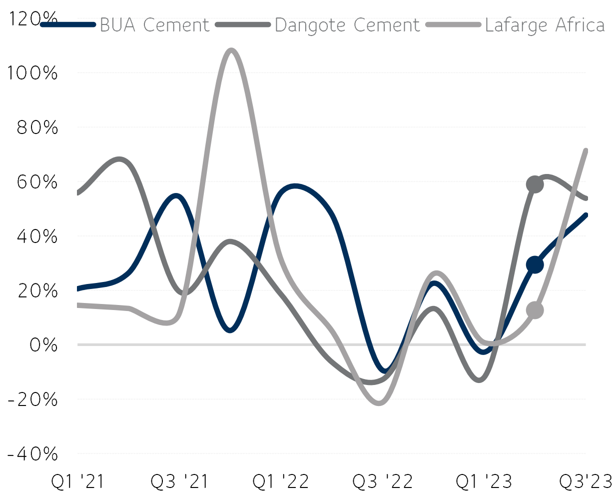


Source: Company data, FBNQuest Capital Research

Profitability trends

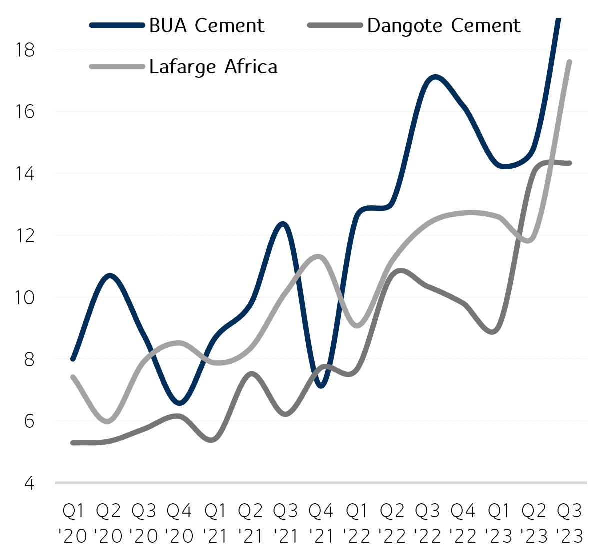
The impact of inflationary pressures on production and operating expenses continued to weigh down on profitability margins, leading to a decline in the average industry gross margin from 46.1% in the previous year to 45.5% y/y. Notably, production and energy costs per tonne increased by 16.9% y/y and 17.7% y/y on average, respectively, in Q3 '23. The drivers remain the growing cost of energy and the player's cost of acquiring raw materials for production. The devaluation of the NGN following the collapse of the FX market segments in Q2 '23 (Jun '23), kept the cost of importation of materials like Gypsum and machine spare parts high.

Production cost per tonne (NGN'000)



Source: Company data, FBNQuest Cap. Research

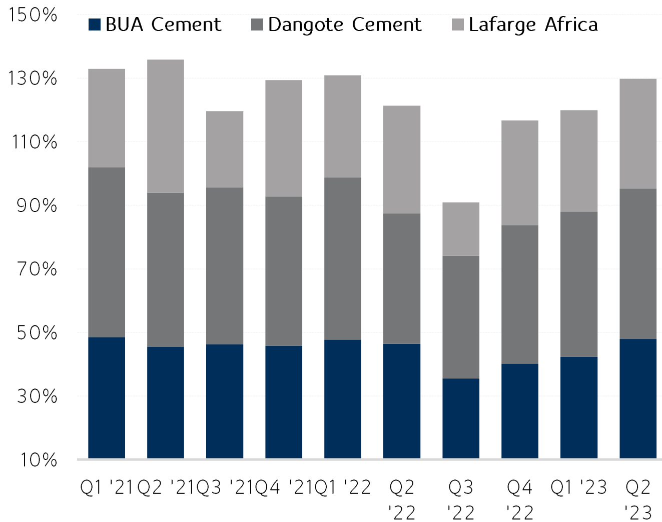
Energy Cost per tonne (NGN'000)



Source: Company, FBNQuest Capital Research

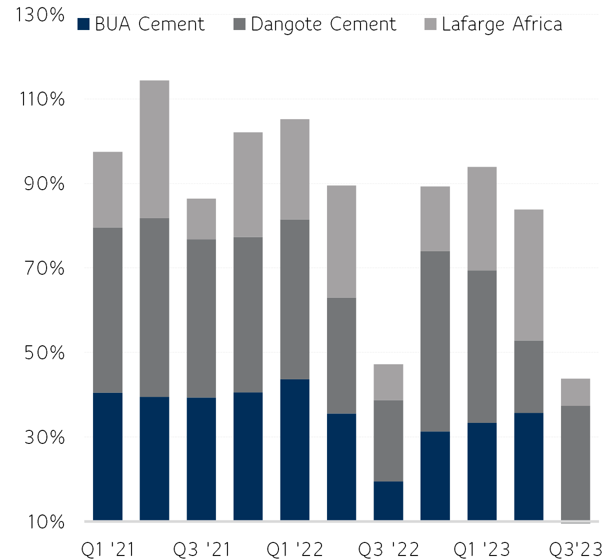
Particularly, DangCem recorded a +42.4% y/y surge in its the cost-to-sales ratio for the 9M'23 period, higher than the 41.1% recorded in 9M'22. This increase was driven by the rises in material costs (17.26% y/y), depreciation charges (32.88% y/y), and fuel consumption (28.91% y/y). Similarly, BUA Cement reported a higher cost-to-sales ratio of 55.5% y/y in 9M'23, up from 54.4% y/y in 9M'22. In contrast, Lafarge demonstrated improved cost efficiency, with the cost-to-sales ratio moderating to 48.8% y/y from 50.1% y/y in the previous year.

EBITDA Margin trend



Source: Company data, FBNQuest Cap. Research

Pre-Tax Margin trend



Source: Company, FBNQuest Capital Research

Notwithstanding, the industry EBITDA margin rose to 43.3% y/y in 9M'23 from 30.3% in 9M'22. Attributable mainly to the growth in revenue. Furthermore, efforts by Lafarge and DangCem to reduce their Co2 emissions and increase adoption of alternative fuel resulted in lower distribution costs and supported the rise in the industry EBITDA margin. Lafarge reported a -7.1% y/y drag in its distribution variable costs following the addition of more gas trucks and the introduction of electric powered trucks to its fleet size, effectively lowering its distribution costs.

Despite reporting higher borrowing costs with an overall industry debt increase of 32.2% to NGN1.4tn in 9M'23, the pre-tax profit for the industry surged by 29.8% y/y, to NGN551.8bn. Particularly, DangCem issued NGN127bn worth of commercial papers, and BUA Cement secured a NGN139.9bn loan from the IFC. This surge in debt contributed to an 86.1% y/y increase in finance costs, reflecting the impact of both new debt inflows and a high-interest rate environment. Consequently, average Q3 '23 profit after taxes increased by 31.9% y/y, a stark contrast to the -44.8% y/y decline in Q3'22. Additionally, except for Lafarge, industry players continued to benefit from pioneer tax incentives during the review period, contributing to the overall positive financial performance.

Outlook

We anticipate improvements in volumes sold in the Q4 '23 period, driven by the onset of the dry season, traditionally conducive to construction and infrastructural activities. The industry's volumes are further expected to receive a boost from BUA's 'Win with the King' promo and DangCem's distributors' promo, spanning both its Nigerian and Pan African operations. We believe the construction industry and by reflection the cement sector is poised for a resurgence, this is hinged on the amount allocated for capital expenditure in the 2024 "Renewed hope budget", which boast of a NGN1.3tn infrastructure allocation. This represents 5.0% of the total expenditure for the 2024E. We note that the overall capital expenditure is -3.0% lower at NGN7.7tn versus the NGN7.9tn allocated in the 2023 budget. However, looking ahead to 2024E, we anticipate that several other factors are projected to drive volumes and contribute to overall profitability growth in what we believe to be a best-case scenario. These include:

1. The anticipation of general economic recovery and the initiation of an infrastructure support fund (ISF) by the Tinubu administration in 2024E.
2. Pricing strategies implemented by the industry players and the potential adoption of concrete technology for road construction when approved by the current administration.

3. The increased adoption of alternative fuels by industry players is expected to have a positive impact on operational efficiency and profitability.
4. The commissioning of BUA's 6MT plants is expected to improve the industry's total installed capacity to 62.8MT and BUA's to 17MT, potentially leading to increased industry volumes.
5. Cement players like DangCem and BUA participating in the African Continental Free Trade Area (AfCFTA) are anticipated to boost export volumes, opening up new markets in Africa and contributing to overall growth.

However, in our view, drivers for a worst-case scenario that would impact profitability includes:

1. Weak macroeconomic environment characterised by the double-digit inflation and high borrowing costs.
2. Higher energy costs per tonne feeding into production and distribution costs.
3. Volatility in exchange rate which would influence operating costs negatively and increase debt stock balance for players with foreign denominated debts.

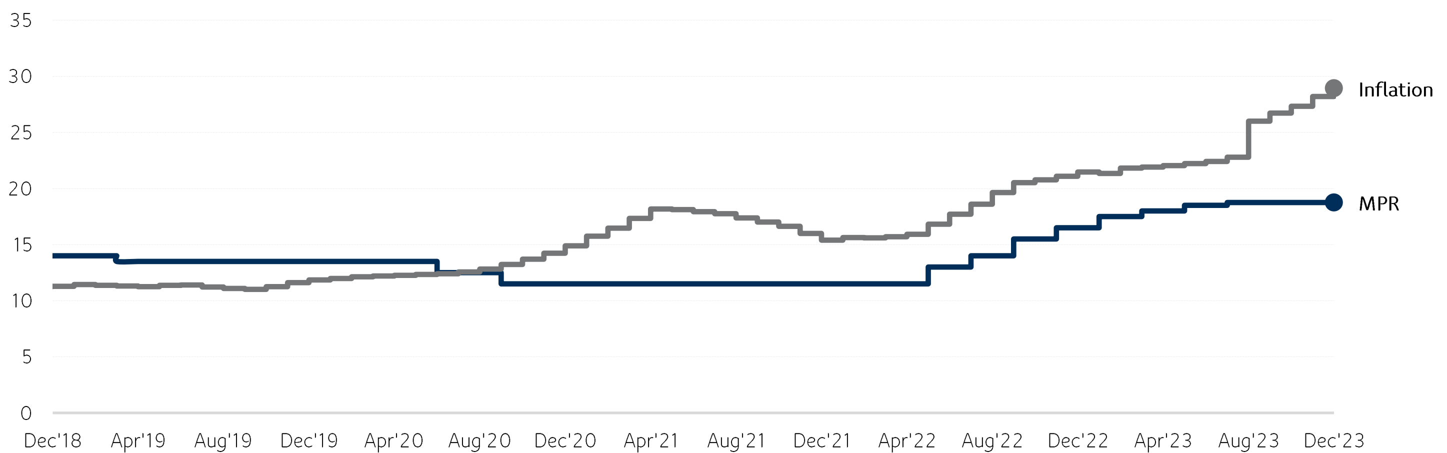
Monetary and fiscal policy

The Monetary Policy Committee (MPC) maintained a restrictive stance through 2023, as the committee raised policy rate by a staggering 225bps. However, the transmission mechanism of previous rate hikes has been rendered largely ineffective due to the CBN's quasi-interventions programmes and financing of fiscal deficits through Ways and Means.

To set a new direction for monetary policy, the new CBN management has signalled its intention to stop the Ways and Means advances to the government, and the execution of monetary policy through quasi-interventionist operations but rather focus on adopting an explicit inflation-targeting framework to improve the effectiveness of monetary policy and reduce the inflationary pressures in the country.

In response to the persistent rise in general price level and excess money supply in the financial system, the CBN implemented several monetary policy measures to ensure price stability and optimal liquidity conditions. The apex bank re-introduced periodical Open Market Operation (OMO) auctions in Oct '23, after been interrupted since Jan '23, enforced regular Cash Reserve Requirement (CRR) debits, removed the NGN2bn limit on funds placed in the Standing Deposit Facility (SDF) for deposit money banks.

Headline inflation and MPR (%)



Source: CBN, National Bureau of Statistics (NBS); FBNQuest Capital Research

Given the upward tracjectory of inflation and the continuous expansion of money supply, we expect the MPC to demonstrate its commitment to combat rising inflationary pressures by tightening monetary policy conditions. Additionally, we anticipate that the CBN will continue the implementation of monetary policy tools to mop up system liquidity, particularly considering the likelihood of fewer MPC meetings in 2024. As such, we expect the MPC to raise interest rate further by c.100bps to 19.75% in 2024.

Inflation still surging ahead

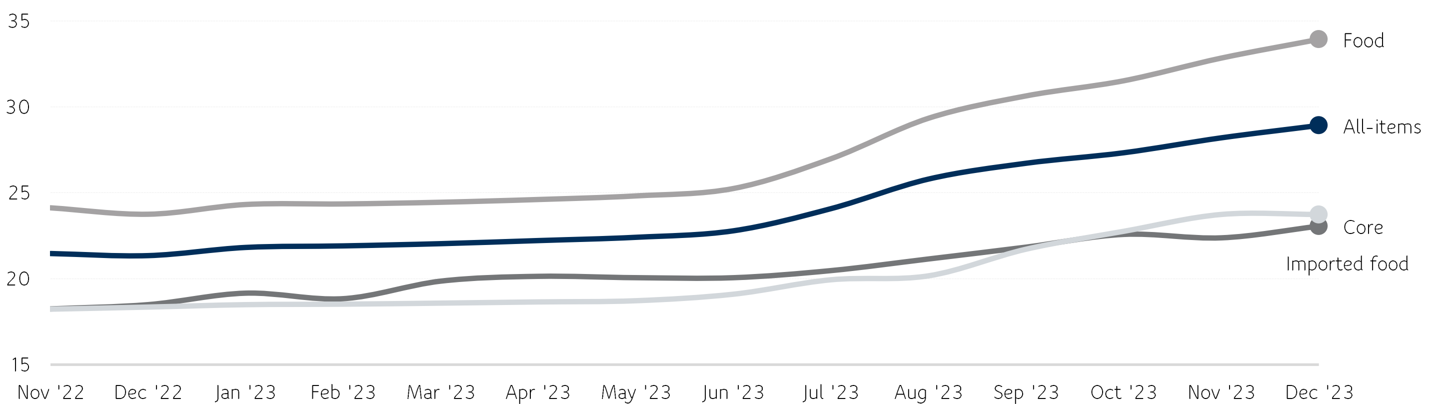
The recent inflation report from the NBS, showed that headline inflation remained on an upward trajectory. The headline reading for Dec '23 showed an increase of 72bps to 28.92% y//y, marking the twelfth consecutive monthly rise. However, the pace of acceleration moderated compared with an increase of 87bps to 28.20 y/y in the previous month. Nonetheless, the Dec '23 reading indicates that the country's inflation rate rose steadily through 2023,

Despite the tightening stance of the monetary policy committee (MPC) in combating the rising inflationary trend in 2023, Nigeria's headline inflation maintained an upward tracjectory through the year. The committee raised the monetary policy rate (MPR) by a significant 225bps and reduced the asymmetric corridor to (+100/-300bps) from (+100/-300bps previously), all as part of sustained efforts to rein in inflation. Additionally, the CBN under the newly appointed Governor, implemented several monetary tools to mop out excess liquidity conditions in the system, including the re-introduction of periodic Open Market Operations (OMO) auctions, removal of the NGN2bn cap on Standing Deposit

Facility (SDF) for banks, and regular Cash Reserve Requirement Debits (CRR) debits. Although these measures resulted in a brief moderation in m/m headline inflation in both Sep '23 and Oct '23, the trend in m/m acceleration was restored in Nov '23 and Dec '23, partly due to festive-induced activities.

The upward trajectory of inflation can be attributed to a combination of structural issues within the agricultural sector and recent reforms by the new administration. These issues include insecurity in food-producing regions, infrastructural deficits, shortage of storage facilities, the deregulation of petrol (gasoline) which led to substantial increase in transportation costs and the depreciation of the Naira due to the removal of restrictions on the fx market. The exchange rate is one of the single-largest drivers of inflation, with major pass-through to items like petrol and other imported items. Consequently, the floating of the naira in Jun '23 resulted in a significant acceleration in consumer prices. For instance, Inflation increased averagely by 102bps between Jul '23 to Dec '23, compared with an average increase of 24bps from Jan '23 to Jun '23. Notably, the sustained rise in the headline inflation rate has weakened household consumption and reduced consumer discretionary spending. Despite the elevated interest rate envrionemt, the significant rise in consumer prices has continued to outpace the increase in yields, resulting in negative real interest rate, thus making investment less attractive.

Consumer price inflation (y/y change, %)



Source: National Bureau of Statistics (NBS); FBNQuest Capital Research

The inflation reading has been mainly driven by a surge in (domestic) food prices due to structural supply-side factors which have continued to cause shocks to food supplies. An additional point is that the pass-through effect of higher transportation costs caused by the increase in petrol prices and the continued depreciation of the naira has also negatively impacted food prices. Notably, food inflation which is the most relevant in Nigeria's CPI inflation basket, has risen consistently since Mar '22, with the exception a brief pause in Dec '22. More specifically, food inflation has increased by a staggering 1,672bps between Mar '22 and Dec '23.

The exchange rate has a significant impact on the core component of Nigeria's inflation basket due to the nation's reliance on imported goods and services and the country's limited financial intermediation. Consequently, imported food inflation has remained elevated. Addtionally, supply disruptions and price shocks from the Russian-Ukrainian war and transmission effect from the naira exchange rate depreciation continues to exert upward pressure on in the imported inflation reading. The latest reading showed that it surged by 115bps to 23.74%. A more worrisome trend is that imported inflation has steadily risen every month since Sep '19.

Although the impact of core inflation on the overall basket is less pronounced, it has continued to trend upward. Excluding brief moderations in both May '23 and Nov '23, core inflation has increased steadily since Mar '23. Notably, the NBS has excluded energy products from the components of core inflation, due to the depreciation of the Naira which has resulted in higher prices of petroleum products. The latest inflation print showed an increase of 68bps to 23.06% in Dec '23.

Inflation outlook

The risks to inflation remain titled to the downside. We anticipate that the transmission effect of the deregulation of gasoline oil and the continued depreciation of the Naira currency to exert upward pressure across core components on the inflation basket. Additionally, we expect continued pressure on domestic prices due to higher transportation costs and persisting insecurity challenges stemming from renewed bandits attacks on farmers in food-producing areas.

However, we anticipate improvements in food security in the country premised on the federal government's efforts to address agricultural insecurity in the country and various government initiatives to boost local food production. Additionally, we expect moderation of the headline reading from mid-2024 due to a combination of high base effect from 2023 and monetary tightening stance by the MPC. Consequently, we forecast headline inflation at c. 21.8% by the end of 2023.

Given the elevated outlook for inflation, we expect the monetary policy authorities to raise interest rates by c.100bps to sustain its efforts in combat anticipated rising inflationary trend. However, we expect to see a decline in inflationary pressures start due to a combination of base effects and in response to the monetary authorities' tightening stance.

Fiscal policy

Macroeconomic policy has shown more weakness on the fiscal front compared to the monetary side. As such, the CBN and the MPC have often been compelled to overcompensate. Over the years, a discernible pattern has emerged wherein the government sets ambitious revenue targets and adjusts capital expenditure to address the revenue shortfalls.

According to provisional data published by the CBN, the FGN recorded a fiscal deficit of NGN9.6trn over 9M '23. When annualised, the fiscal deficit is equivalent to c. 5.6% of the projected 2023 GDP, roughly unchanged from the fiscal deficit in 2022. It is important to note that this deficit exceeds the 3% of GDP limit set by the Fiscal Responsibility Act. The primary reason for the persistent revenue shortfall is the poor performance of the oil sector, which is experiencing issues with low productivity. As a result, oil revenue accruing to the federation account amounted to c. NGN3.0trn over the 9M '23 period, representing a 14% shortfall compared to the pro-rata revenue benchmark of NGN3.5trn. In contrast, the non-oil revenue outturn of NGN6.7trn exceeded the budget benchmark of NGN5.7trn.

Looking ahead, we anticipate an expansion in the FGN's revenue profile for 2024 due to the recent reforms carried out by the Tinubu administration which include:

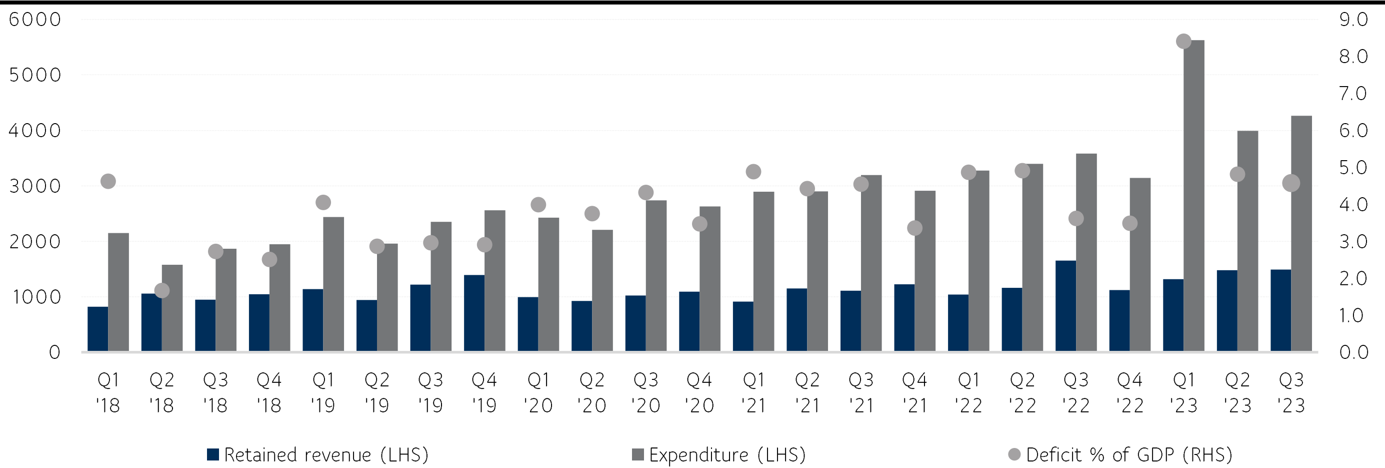
1. A decrease in petrol subsidies
2. The devaluation of the naira
3. Reforms aimed at improving tax revenue

As a result of the expected increase in revenue, the FGN forecasts a lower fiscal deficit of NGN9.2trn for 2024. This represents c.3.9% of projected 2024 GDP, compared to a 5.6% forecast for 2023. Underpinning the fiscal deficit are planned expenditure and revenue of NGN28.8trn and NGN19.6trn, respectively. These compare with the NGN24.8trn and NGN11.0trn expenditure and revenue budgets for 2023.

The FGN also anticipates a boost in revenue from an increase in oil production to about 1.78mb/d, as per the assumptions made in the 2024 budget. However, due to the persisting problems related to low oil productivity in the Niger-Delta region and the lack of investments made by the International Oil Companies (IOCs) in recent years, we remain cautiously optimistic about this development.

Despite the projected rise in revenue, we expect a significant proportion of the gains from the higher revenue to be partially offset by an increase in workers' salaries and other administrative overheads. Another pressure point is the potential rise in external debt service costs arising from the sharp downward adjustment of the naira, which has expanded the external debt component in local currency terms to c.NGN32trn as at Q3 '23 from NGN19.6trn in Q1 '23. All these factors are expected to put further strain on the fiscal space.

Fiscal operations of the FGN (NGN'bn)



Source: CBN, FBNQuest Capital Research forecast

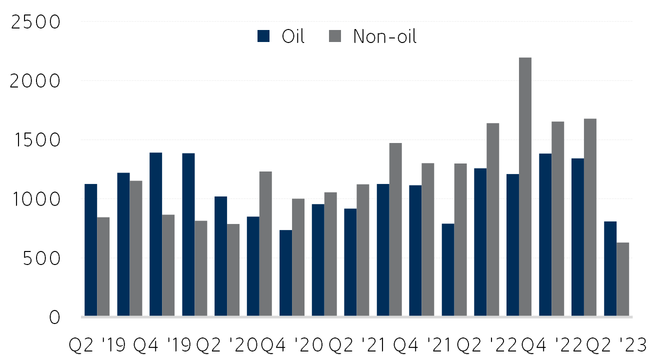
The devaluation of the naira exchange rate to approximately NGN760/USD in Jun '23, from around NGN460/USD previously, has led to an expansion of revenue disbursements to the three tiers of government, including the federal government. However, we anticipate additional pressure on the fiscal space from three different factors:

1. A rise in govenments wage bill
2. The apparent reinstatement of fuel
3. Higher debt services costs.

We expect most of the gains from higher revenue to be partially offset by the imminent increase in government personnel costs due to ongoing salary negotiations with trade and labor unions.

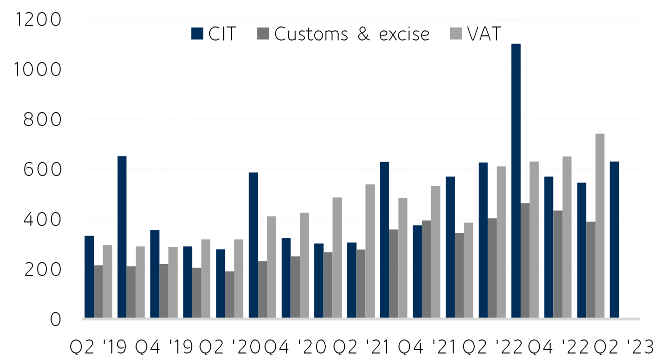
President Tinubu announced the elimination of fuel subsidies during his inaugural speech on 29 May '23. The scraping of subsidies initially resulted in monthly savings of approximately NGN400 bn. Despite the lack of acknowledgment from the FGN, fuel subsidies appear to have been reinstated, driven mainly by the sharp depreciation of the naira exchange rate to over NGN1,400/USD on the official window.

Federally collected revenue (NGN'bn)



Source: CBN, FBNQuest Capital Research

Federally collected non-oil revenue (NGN'bn)

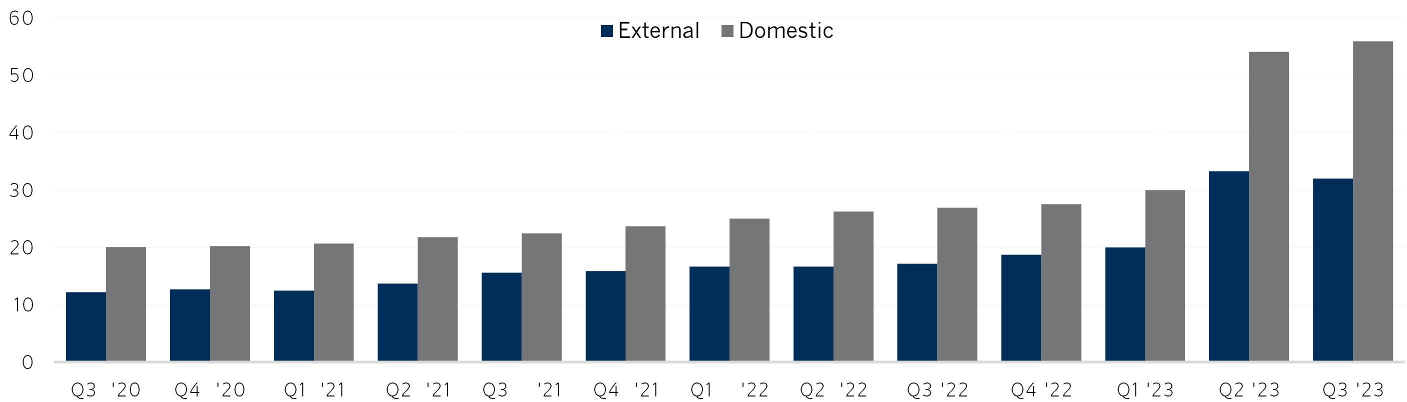


Source: CBN, FBNQuest Capital Research

A marginal rise in public debt stock

According to the most recent data from the Debt Management Office (DMO), the nation's overall debt stock increased slightly by c.1% q/q to NGN87.9trn in Q3 '23. However, on a y/y basis, the rise in the total public debt was more significant, doubling y/y. The marginal q/q rise in the debt burden was primarily due to an increase of 3% q/q in the domestic debt stock to NGN56.9trn. Conversely, the FG external debt obligations reduced by -4% q/q or -USD1.6bn q/q to USD41.6bn in Q3 '23. In terms of composition, the domestic and external debt components make up for roughly 64% and 36% of the total public debt, respectively. This compares with a target domestic:external split of 70% to 30% proposed in the DMO's debt management strategy for 2020 to 2023.

Public debt stock (NGN tn)



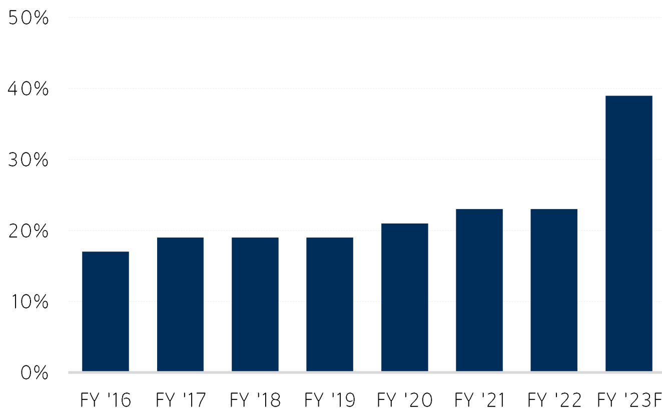
Source: Debt Management Office (DMO), FBNQuest Capital Research

On a standardised basis, the country's total public debt stock implies an estimated debt-to-GDP (2023f) ratio of c.39%, slightly higher than the 38% estimate recorded in Q2 23. The total public debt measure covers the federal and state governments' external and domestic debt stock. In terms of implications, the forecast debt-to-GDP ratio of 39% points to a limited borrowing headroom, particularly when we consider the 40% debt ceiling stated in the agency's Medium-Term Debt Management Strategy.

The FGN's total domestic debt stock increased by 4% q/q to NGN50.2trn in Q3 '23. On a y/y basis, the nation's domestic debt stock more than doubled y/y, primarily due to the inclusion of NGN22.7trn ways and means advances obtained by the federal government from the CBN into the overall public debt stock. The FGN's share of domestic debt represents 90% of the nation's total domestic debt stock of NGN55.9trn, with the balance comprising of the domestic debt of the state governments and the federal capital territory (FCT). The FGN's total domestic debt stock is equivalent to roughly 22% of 2023f GDP. However, if we include the domestic debt of the states and the FCT, the figure rises to 24.6% of '23f GDP.

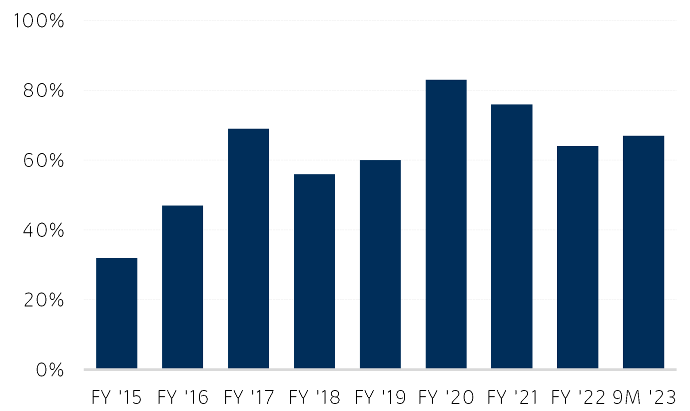
In contrast, the the FGN's total external debt stock decreased by approximately USD1.6bn in Q3 '23 compared with the previous quarter to USD41.6bn. The decrease was primarily due to the FGN's repayment of USD1.6bn in promissory notes, the redemption of a USD500m Eurobond maturity, and a USD440m reduction in the debt owed to the IMF. These were offset by smaller increases in the FGN's debt obligations to other lenders. Based on standardised metrics, the total external debt is roughly equivalent to c.14% of 2023f GDP. The external debt stock comprises the external borrowings of the federal government and those of th 36 state governments and federal capital territory, for which the federal government typically provides sovereign guarantees.

Total public debt to GDP (%)



Source: NBS, DMO, FBNQuest Capital Research

Debt service-to-revenue (%)



Source: Ministry of Finance Budget and Planning, FBNQuest Capital Research

Going forward, we anticipate a rise in the country's total debt stock for several reasons. The 2024 budget proposal forecasts an estimated budget deficit of NGN9.2trn, of which NGN6.0trn will be sourced from the domestic market, while the FGN plans to borrow about NGN1.8trn (USD2.2bn) from external sources. Regarding the domestic market, the DMO will be expected to auction FGN bonds on a monthly basis to plug the budget deficit, following its record debt issuance sales of NGN5.3trn in 2023. Another factor is the expected inclusion of the securitization of an additional NGN7.3trn ways and means advances from the CBN, after the President's request was granted by the Senate. Furthermore, due to the CBNs commitment to address the fx liquidity challenge and the resultant devaluation of the naira, we expect the FGN to source for external borrowing as a potential short-term fix to address the liquidity crisis and stabilze the currency on the foreign exchange rate market.

The country's growing debt profile heightens concerns regarding its long-term sustainability, particularly considering underperforming revenues. The current precarious fiscal situation has led to the reassessment of the country's fiscal policies by the new administration. While we commend the new administration's initiatives and policies to broaden the tax base in order to increase the country's revenue-generating capacity, there is still a lot of ground to cover to reduce the fiscal deficit and the country's reliance on new borrowings.

Exchange rate and official reserves

Historically, Nigeria's monetary policy makers favoured a stable fixed exchange rate for the NGN due to its significant impact on domestic inflation. This mindset had a significant influence on the actions of the central bank and the MPC. However, during the tenure of the suspended former CBN governor, *Mr Godwin Emefiele*, the strict adherence to a fixed exchange rate policy led to multiple exchange rate windows for different market segments. Unfortunately, this caused a considerable disparity between the official and parallel exchange rate markets, resulting in a premium of over 60% for the latter compared to the former.

During his presidential campaign, *President Tinubu* promised to implement a thorough revision of monetary policy in order to achieve exchange rate unification. As a result, there were widespread expectations that the monetary authorities would start the process of converging exchange rates following the President's election victory

Despite the anticipated unification of exchange rates, the financial markets experienced disruption when the central bank, in mid-Jun '23, consolidated all exchange rate market segments into the Nigerian Autonomous Foreign Exchange Market (NAFEM) – formerly known as the investors and exporters (I&E) window. This announcement heightened volatility in the foreign exchange markets because the removal of forex trading restrictions marked a notable shift in the central bank's foreign exchange policy. As a result, the official exchange rate on the I&E window initially decreased to NGN664/USD from NGN461/USD before stabilising at NGN760/USD by the end of Q2 '23.

Some of the operational changes to the fx market announced by the CBN in Jun '23 included:

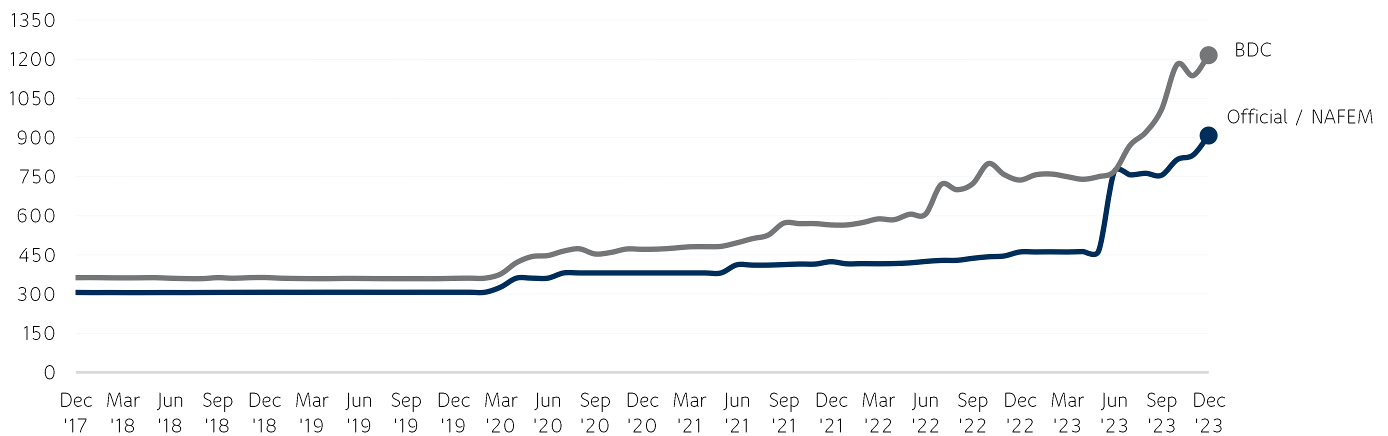
1. Abolishment of all fx market segments and their consolidation into NAFEM.
2. Re-introduction of the "willing buyer, willing seller" model.

3. Re-introduction of order-based two-way quotes with bid ask spread of NGN1.
4. The removal of trading caps on the NAFEM window to allow for the free float of the naira exchange rate.
5. The proscription of trading limits on oversold FX positions and nil on overbought positions.
6. The re-introduction of order books to ensure transparency of orders and seamless execution of trades.

After assuming office as the new governor of the Central Bank of Nigeria (CBN), Olayemi Cardoso implemented additional reforms to the foreign exchange market. In Oct '23, the CBN lifted the market restrictions on 43 items that were previously not eligible for fx access. This move was aimed at reducing segmentation within the market, and promoting a more open and competitive environment.

As illustrated in the chart below, the fx reforms, which bagan in Jun '23, initially resulted in a near closure of the arbitrage gap of almost NGN300 between the official and parallel markets. However, the parallel market premium has since re-emerged, with the naira now trading around NGN1,400/USD. Despite the naira being allowed to float, there has not been a significant improvement in fx liquidity. Consequently, in 2023, the naira depreciated by approximately 48%, ending the year at NGN907.1/USD. The fx rate is currently hovering around NGN1112/USD

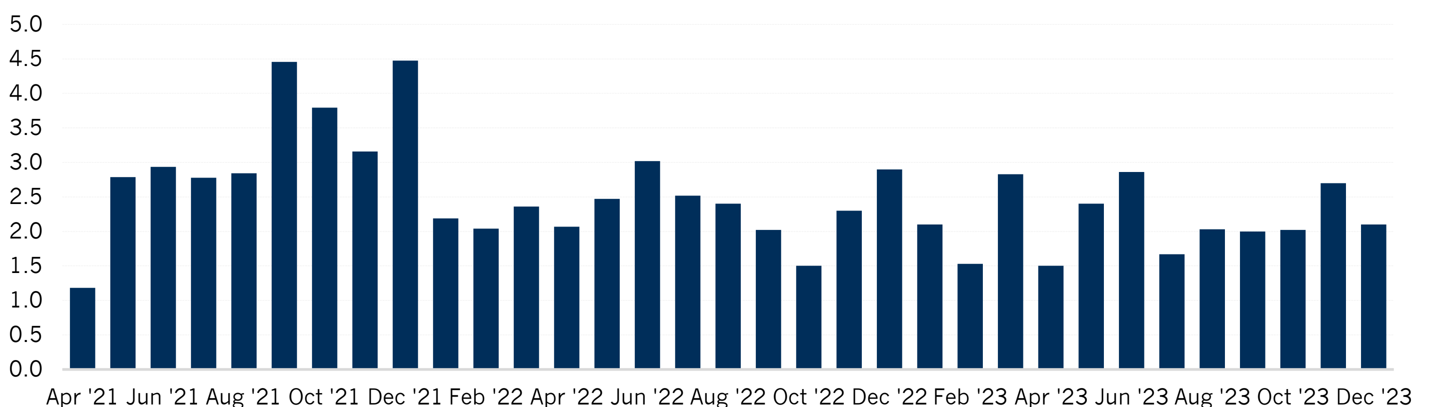
Operational changes to the fx market



Source: CBN, FBNQuest Capital Research

Based on FMDQ data, the foreign exchange market turnover on the NAFEM window (previously - importers' and exporters' (I&E) window averaged approximately USD2.1bn in 2023, down from roughly USD 2.3bn in 2022. Clearly, there has not been a significant inflow of foreign currency from the offshore investment community. Due to the limited foreign portfolio investors (FPI) inflow, non-bank corporations and exporters have consistently made up about 70% of the total value of foreign exchange inflow in the Investors and Exporters (I&E) market in recent times.

NAFEM monthly fx market turnover (USDbn)



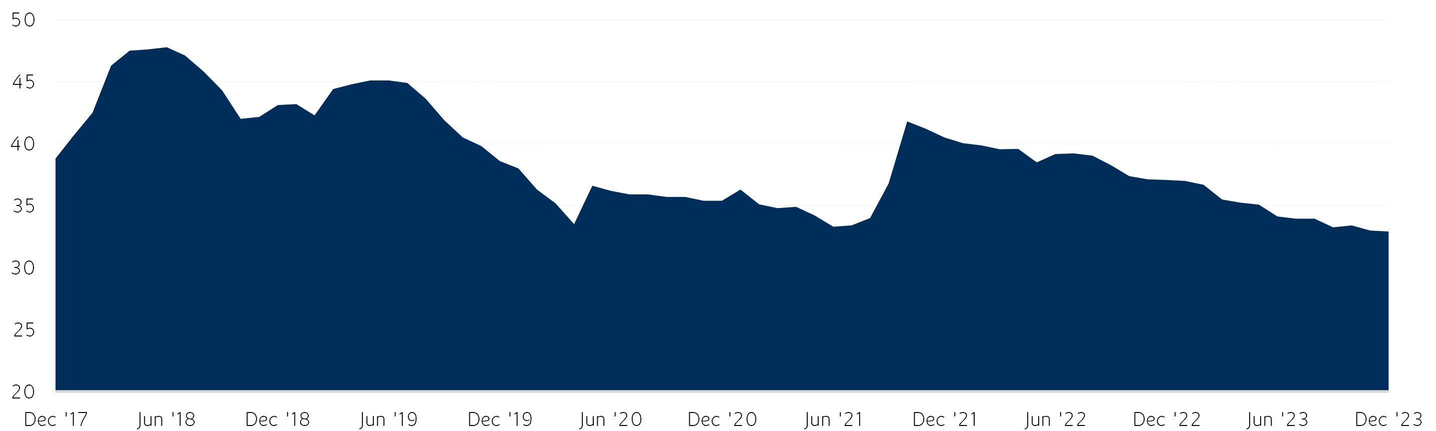
Source: CBN, FBNQuest Capital Research

As the fx market continues to determine an appropriate pricing for the naira, we anticipate sustained volatility in the naira exchange rate this year. Based on the existing scenario, our projection indicates a year-end NAFEM/I&E rate of NGN1,317/USD. However, there is a potential upside risk with the possibility of improved forex liquidity, driven by the concerted efforts of the fiscal and monetary authorities to attract foreign inflows into the economy. These inflows could come from sources such as the proposed securitisation of NLNG dividends, expected to generate around c. USD7bn, and bilateral engagements with countries like Saudi Arabia and the UAE, which could result in substantial multi-billion-dollar investments in the economy. Notably, the federal government in Dec '23 received a USD2.3bn foreign exchange support facility from the African Import-Export Bank.

Sustained decline on the gross official reserves

Nigeria's gross official reserves have been steadily decreasing since Oct '21 when they briefly climbed to USD41.8bn, thanks to factors such as the IMF's SDR allocation of USD3.3bn, a USD4bn Eurobond issuance, and at the time, rising oil prices. However, according to data from the CBN, the total reserves decreased by USD4.2bn in 2023, indicating an average monthly depletion rate of about USD348m.

Official reserves (USD'bn, 30-day moving averages)



Source: CBN, FBNQuest Capital Research

Total reserves at the end of Dec '23 covered 7.7 months of merchandise imports per the balance of payments (BoP) for the 12 months to Jun '23 and 5.7 months when we add imported services. While this may suggest an improvement compared to the 7.1 months of merchandise import cover and 5.3 months of total import cover (including services) as of H1 '23, it is important to note that the improvement is due to limited accessibility to foreign exchange for importers. Noteworthy is the 14% y/y decline in total merchandise imports to USD51.6bn for the 12 months ending Jun '23 - the period used to calculate the import cover – compared with the USD60.0bn for the year earlier period ending Jun '22.

However, for a more accurate assessment, it is essential to adjust the gross reserve figure (including the import cover) to account for the pipeline of delayed external payments and the encumbered portion of the reserves. The CBN's publication of its audited accounts last year after an extended non-disclosure period revealed the possibility that the encumbered portion of reserves may surpass initial estimates. For instance, the 2022 accounts disclosed a securitised loan of about USD7.5bn owed to JP Morgan and Goldman Sachs, in addition to fx forwards totaling almost USD7bn. Despite the lack of clarity from the CBN regarding the exact proportion of unencumbered external reserves, the 2022 accounts suggest a potential encumbrance of at least half of the reserves balance.

Late last year, the central bank began a gradual process of addressing the backlog of outstanding fx forwards, aligning with the commitment made by *Governor Olayemi Cardoso*. As reported by the bank, approximately USD2bn worth of matured fx forwards have been successfully cleared since the initiation of this effort in Q4 '23, reducing the total outstanding balance from USD7bn. Additionally, the CBN recently managed to clear USD62m of the USD700m funds trapped in the country belonging to foreign airlines. Although these payments may appear relatively modest compared to the outstanding balance, they underscore the CBN's commitment to tackling some of the persisting forex issues.

Despite the CBN's move to float the NGN in Jun '23, attracting foreign exchange inflows has proven challenging, largely attributed to the cautious approach taken by offshore investors. Recent data from the NBS reveals a significant decline of -44% y/y, with the total value of capital imported into Nigeria reaching a meager USD654m in Q3 '23. This contrasts with an average quarterly figure of USD5.0bn in the eight quarters before the COVID-19 pandemic started in Q2 '20.

A weaker outlook for the balance of payments

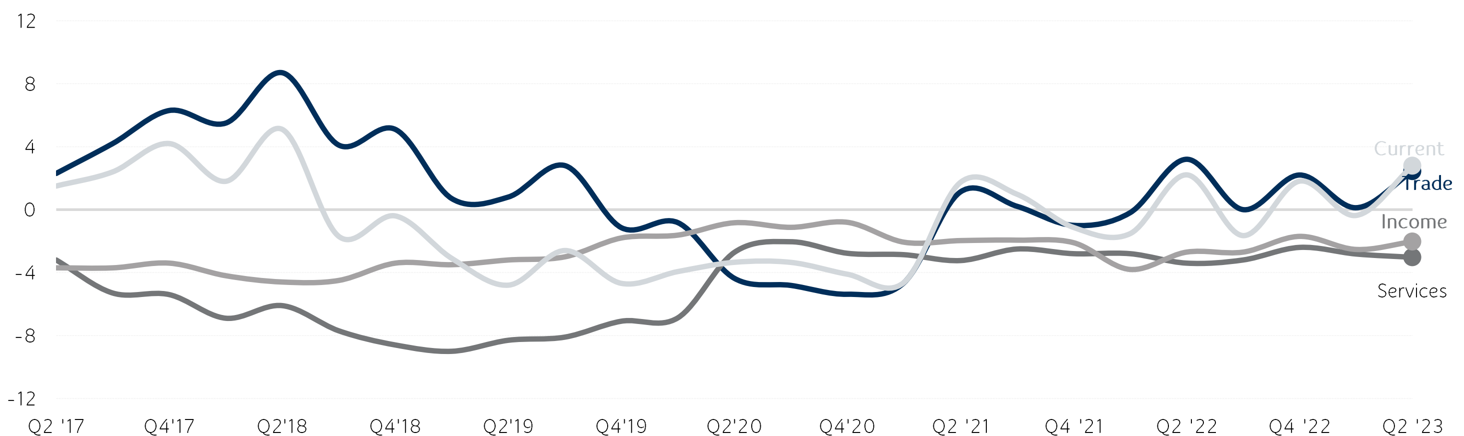
Looking ahead, we anticipate limited accretion to the external reserves this year, primarily driven by the challenges in raising Nigeria's crude oil output, which accounts for over 80% of the country's merchandise export earnings. The current production stands at approximately 1.3 million barrels per day (mb/d), excluding condensates, compared to a historical average of well over 1.7 mb/d. Despite the federal government's ambition to increase oil production to 1.78 mb/d, as outlined in the 2024 budget, we maintain cautious optimism due to persistent issues surrounding oil theft in the Niger Delta and lack of investments in the sector.

Concerning pricing, anticipated production cuts by OPEC member countries will likely be offset by higher oil output from non-OPEC producers, particularly the expected increase in US oil production to around 13.1 mbpd from 12.9 mb/d in 2023. This is likely to keep oil prices in equilibrium. However, heightened geopolitical risks, especially in the Middle East, could potentially constrain the region's oil exports, particularly those from Iran. With these factors considered, we project the gross official reserve balance to be around USD34.0bn by the end of 2024, slightly higher than the USD32.9bn registered in 2023.

A marginally surplus current account balance

We anticipate Nigeria will achieve a modestly positive current account (CA) surplus of 0.1% of GDP in 2024, slightly lower than the projected 0.2% surplus for 2023. Despite the current account balance fluctuating between surpluses and deficits over the last eight quarters, we foresee a shift to surplus in 2023 due to reduced imports resulting from fx liquidity challenges. Looking forward, we anticipate the ongoing issues with foreign exchange access will continue to restrict import trade for most of 2024. Additionally, the (partial) removal of petrol subsidies and the subsequent increase in pump prices will result in a lower volume of petrol imports and decrease the overall import bill. We expect the current transfers account, which has historically been supportive of the current account balance, to sustain its trend of surpluses, thanks to inbound diaspora remittance inflows.

Trends on the balance of payments (BoP; % GDP)



Sources: CBN; FBNQuest Capital Research

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Updated: 05 Feb. 24

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Rating	General Equities
OUTPERFORM	The analyst expects the stock to outperform the Nigerian Stock Exchange (NSE) All Share Index over the next 12 months or the specified investment horizon.
NEUTRAL	The analyst expects the stock to perform in line with the NSE All Share Index over the next 12 months or the specified investment horizon.
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ASSET ALLOCATION	The recommended weighting for equities, cash and fixed income instrument is based on a number of metrics and does not relate to a particular size change in one variable.

Rating distribution for Nigeria listed equities rating

As at 05 Feb. 24	Total FBNQuest	
Recommendation	Count	% of Total
OUTPERFORM	7	30.4
Neutral	14	60.9
Underperform	2	8.7
Total	**23**	**100**

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