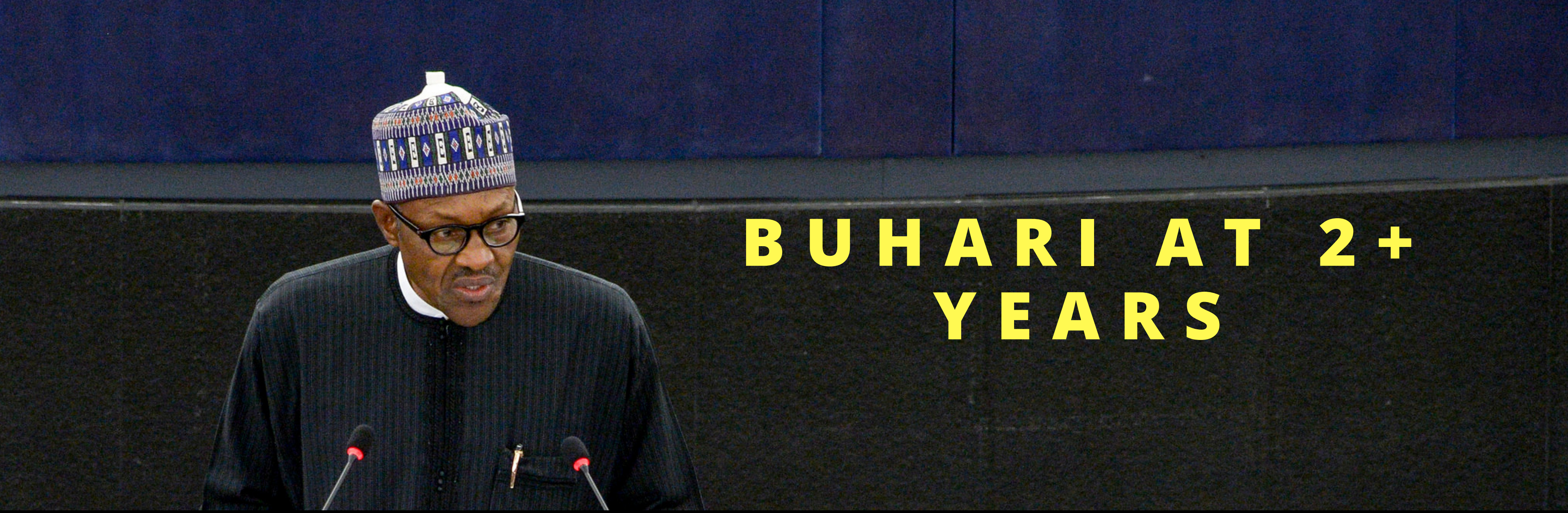
QUANTEXTIVE

NIGERIA

2017 IN REVIEW

CONTENTS



BUHARI AT 2+ YEARS

President Muhammadu Buhari of the All Progressives Congress (APC) was in May 2015 sworn in on a powerful 'change' mandate centered on countering Islamist militant group Boko Haram in northeast Nigeria, stemming corruption, and strengthening the economy. Buhari's position was bolstered by popular support, but expectations were high given his assumption of leadership of a country facing significant challenges in its economy, security and profile for investors.

These problems were at base a result of its dependence on sales of crude oil to finance government spending, over-reliance on government spending as a driver of productivity and employment, historic misuse and theft of oil earnings by public officials, and significant, highly-visible inequalities of wealth and opportunity. Almost three years into Buhari's government, there have been clear successes in counter insurgency efforts, one of his administration's of three principal priorities. However, there are mixed results pertaining to the anti-corruption campaign, and a marked failure where the economy is concerned, which this article explores.

MIXED RESULTS IN THE ANTI-CORRUPTION DRIVE

The anti-corruption campaign is one of the centerpieces of the Buhari administration—a campaign made more urgent by the poor state of public finances and the plan to channel recovered misappropriated funds towards targeted spending on critical sectors. Indeed, the government has been successful in reinvigorating the Economic and Financial Crimes Commission (EFCC), which has demonstrated an unprecedented level of activity under Buhari.

The anti-graft agency has launched a series of investigations into public officials from the previous government, in particular, former cabinet officials, state governors and senior civil servants. However, to-date, that's where the EFCC's effectiveness ends. The agency has failed to secure a single conviction, a failure partly attributable to limitations in resources, and its current capabilities and capacity.

Buhari's anti-corruption campaign has come under criticism for being highly politicised; a populist measure intended to distract from government struggles to meet budget commitments. Critics of the anti-corruption campaign have alleged that it is focused on senior officials from the People's Democratic Party (PDP) era and the president's personal adversaries, whereas members of the APC have escaped the same level of scrutiny.

DOING BUSINESS IN NIGERIA

Nigeria retains a reputation for entrenched petty and high-level corruption, and doing business in the country generally entails significant integrity risks. The country was ranked 136 out of 168 countries with a score of 28/100 in Transparency International's 2016 Corruption Perception Index. While the rank remains unchanged from 2015, the score reflects a two-point increase from 26.

Similarly, the World Bank 2016 Worldwide Governance Indicators (WGI) ranked Nigeria 9.1/100 (up from 7.2 in 2015) in the control of corruption—'reflecting perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption'.

CORRUPTION PERCEPTION INDEX

136

28/100
TRANSPARENCY SCORE

OUT OF 176 RANKED COUNTRIES

Transparency International's 2016 Corruption Perception Index

CONTROL OF CORRUPTION SCORE

9.1/100

World Bank 2016 Worldwide Governance Indicators

"reflecting perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption"

Almost
1/3
of Nigerian adults pay bribes when in contact with public officials

Almost one bribe is paid by every adult Nigerian each year

EXCERPTS FROM

National Bureau of Statistics report

CORRUPTION IN NIGERIA
BRIBERY: PUBLIC EXPERIENCE AND RESPONSE

2017

About
₦400 billion
the equivalent of 39 percent of the country's combined federal and state education budgets in 2016–is spent on bribes each year

Bribe payers spend
1/8
of their salaries on bribes

ONGOING ANTI-CORRUPTION EFFORTS

In what could loosely be deemed an apparent acknowledgement of the shortcomings of the anti-corruption campaign, Buhari on 7 December said "the fight against corruption is the most difficult task on the present administration's agenda since its inception over two years ago". He also reportedly asked Nigerians to be patient with him as he seeks to follow due process and respect human rights.

"the fight against corruption is the most difficult task on the present administration's agenda since its inception over two years ago"

CORRUPTION EFFORTS IN 2018

In the coming year, the EFCC is likely to push ahead with its investigations into former public officials, the deals they agreed and how funds were used. Further accusations and arrests will provide an indication of momentum in the government's anti-corruption drive. The authorities are likely to pressure individuals under investigation to seek plea bargains, and will either seek to renegotiate terms or cancel licenses with commercial entities found to have engaged in corrupt activities under the previous administration or significantly breached contracts.

In the longer term, the government will seek to reform the EFCC to improve its capacity and effectiveness. The Buhari administration will only be able to claim the anti-corruption drive as a success when convictions are secured and fines and prison sentences are handed down by the courts.

PATH TO RECOVERY

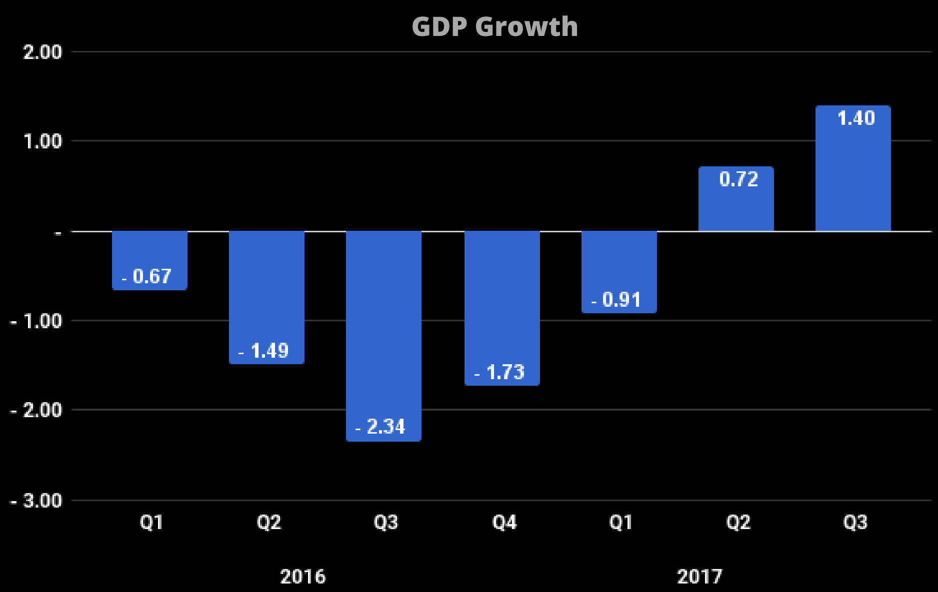
The Buhari administration's economic policies, or lack thereof, failed to adequately navigate Nigeria through the global oil price decline. The government's medium term economic strategy, the Economic Recovery and Growth Plan (2017-2020), was not launched until March 2017.

ECONOMIC RECOVERY

In 2016, global oil prices hit a 13-year low of approximately USD 27 per barrel. This phenomenon combined with shortfalls in anticipated oil production amid a resurgence of violence in the oil-producing Niger Delta region, operational issues, weak transparency mechanisms and the mismanagement of long-term savings, meant that windfall revenues from the period of oil prices hovering around USD 100 per barrel had not been adequately ring-fenced.

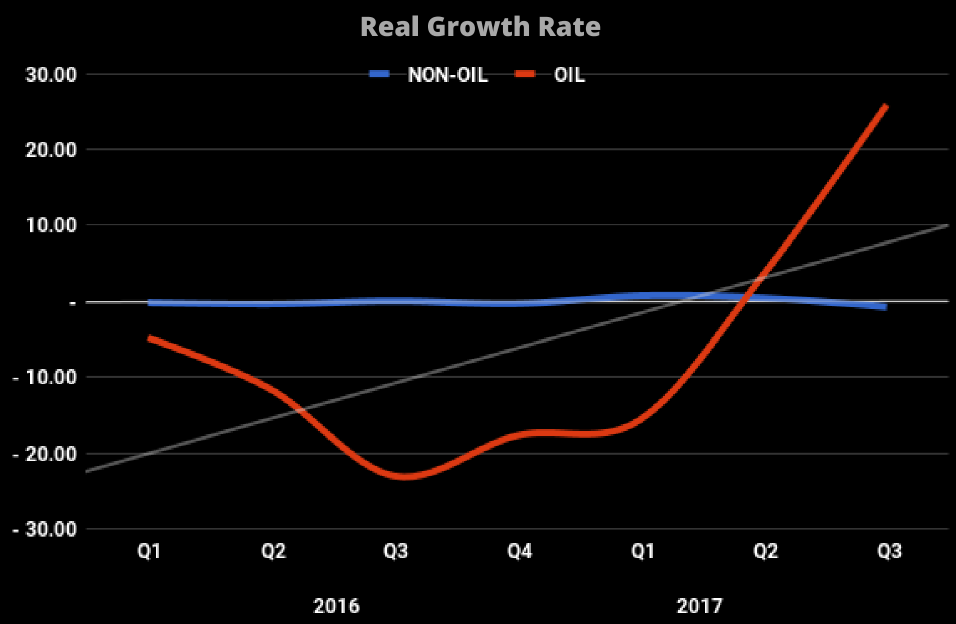
The oil-dependent country experienced its first full-year recession in 25 years with a negative growth of 1.5 percent in 2016. Lower foreign exchange earnings from oil exports had spillover effects on non-oil sectors. This translated into untold hardships for Nigerians, many of whom saw their purchasing power plummet and struggled to keep up with increased costs for food, services and transportation, amid unpaid or delayed salaries and pensions. Furthermore, businesses recorded significant drops in turnover, profit margins and capacity utilization, resulting in massive layoffs. NBS figures from its June unemployment report pegged the unemployment rate at 14.2 percent in the fourth quarter of 2016, up from 13.9 in the preceding quarter.

GDP OVERVIEW



Data from National Bureau of Statistics Report GDP Q3 2017

The NBS Q3 GDP report released on 20 November stated the Q2 growth rate as 0.72 percent, largely based on oil sector growth, and stated that GDP grew by 1.4 percent in Q3. This represents growth 3.74 percentage points higher than the rate of -2.34 percent recorded in the corresponding quarter of 2016.



The non-oil sector contracted by 0.76 percent in Q3, -1.20 points lower than the preceding quarter of 2017, and down by -0.79 percentage points from Q3 2016—with contractions in manufacturing, construction, trade, transportation and storage, and information and communications. The decline in the non-oil sector indicates that the country's recovery has been largely driven by oil; consequently, any shocks in the oil industry has the potential adversely impact the economy.

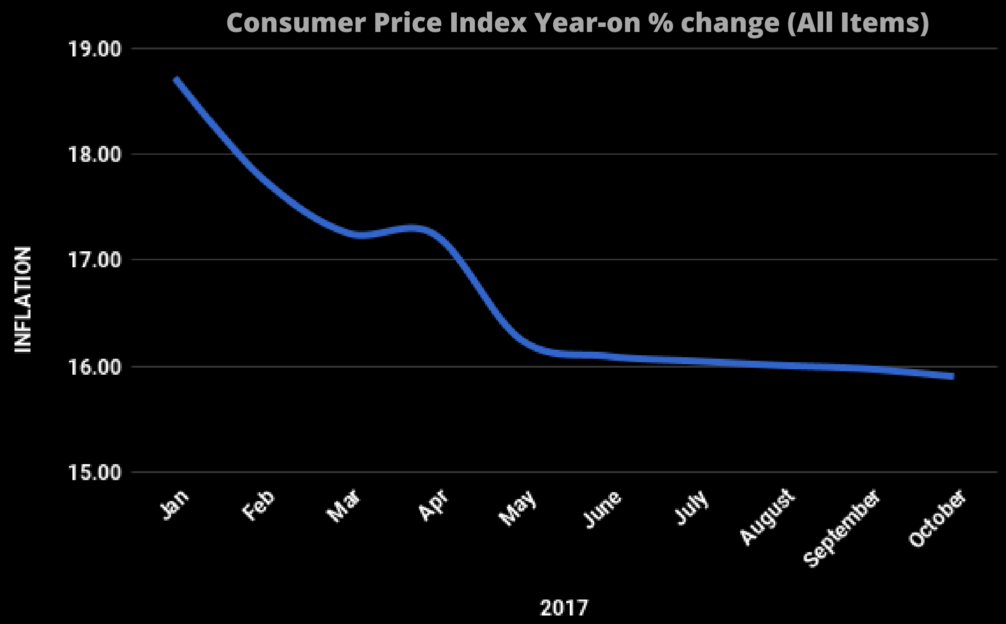
FOREIGN EXCHANGE RESERVES

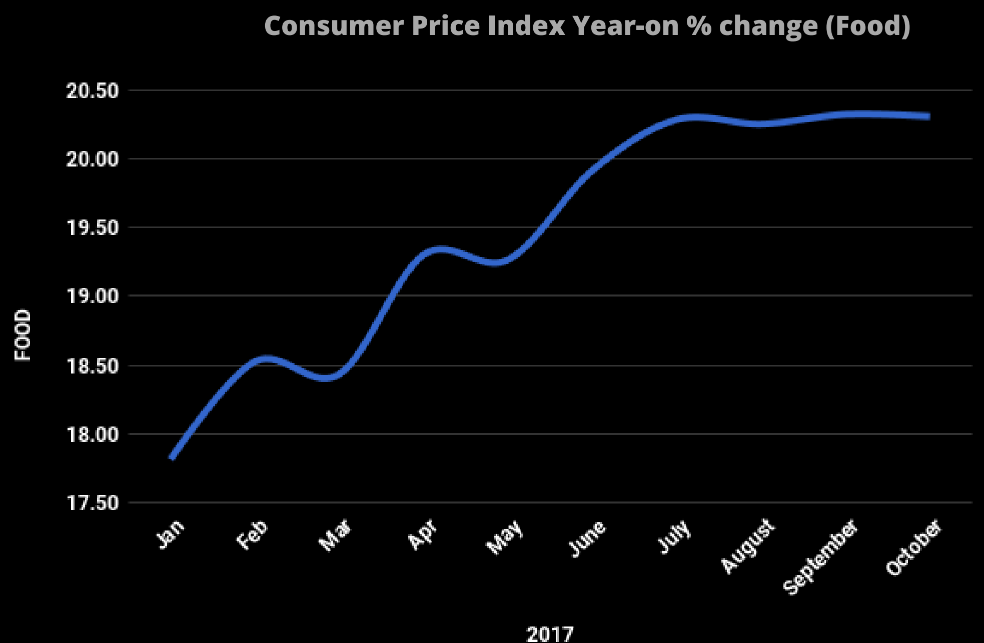
Increased revenue from oil has had a positive impact on foreign exchange reserves. The Central Bank of Nigeria (CBN) data from 6 December shows that foreign exchange reserves stood at USD 35.73bn, up from USD 34.02bn a month prior, and USD25.84bn at the end of 2016. This represents a 38 percent increase over the past 11 months, but remains almost less than half of the peak of USD 68 billion in August 2008.

ON INFLATION

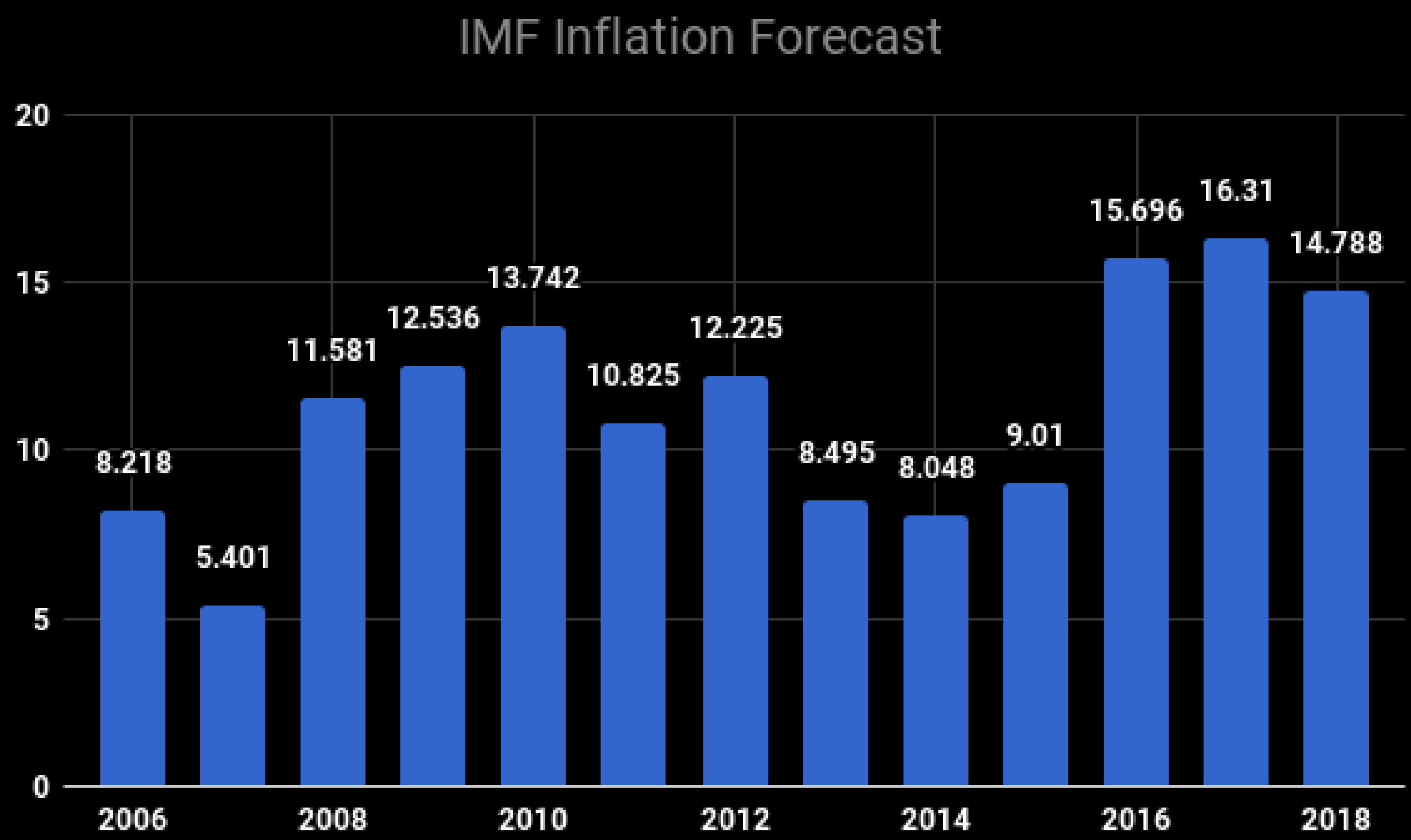
Inflation appears to be easing, as figures from the NBS Consumer Price Index (CPI) report released on 15 November indicates that inflation decreased to 15.91 percent in October, from 15.98 percent in September, 16.01 in August and 18.72 in January. Although inflation slowed for the ninth consecutive month this year, it remains in excess of the government's target of 6-9 percent.

Additionally, food prices increased by 20.31 percent year-on-year in October, a marginal decrease by 0.01 percent from September, and compared to 20.25 percent in August—sustaining the upward trend in food inflation in 2017. The rise in food prices in October was largely driven by the costs of bread and cereals, meats, oils and fats, vegetables and fish, amongst other items, according to the NBS.





ON INFLATION (CONTD.)



CBN Governor, Godwin Emefiele, expects the inflation rate to fall at a faster pace and approach the high single digits by the middle of 2018. However, the IMF, in its World Economic Outlook from October, expects that inflation will remain in the double digits next year and forecasts an average inflation rate of 16.3 percent in 2017 and 14.8 percent in 2018. The IMF anticipates the high rate of inflation will be sustained by "persistent effects of past inflationary shocks from sharp currency depreciations, higher electricity and fuel prices, and an accommodative monetary policy".

EXCHANGE RATES

Meanwhile, the CBN continues to run a convoluted exchange rate system as it attempts to control the Naira, rather than let it float freely. The central bank regularly injects millions of dollars into the interbank foreign exchange market to boost liquidity and alleviate dollar shortages. This was most recently the case on 20 November, 7 November and 31 October, when it injected USD 210 million, USD 195 million, and USD 195 million, respectively.

The CBN continues to quote the Naira at about 305 to the dollar, however, it has for several months been hovering at around 360 to the dollar for investors, about the same level as in the parallel market. In the medium term, the government expects the Naira to strengthen and does not foresee devaluation, according to a statement from Finance Minister Kemi Adeosun on 2 November.

2018 ECONOMIC FORECAST

Over the next year, the recovery in oil production and inward investments will positively impact economic growth. The government will continue to pursue efforts to recover misappropriated funds, and broaden the tax base, while investing in infrastructure projects as a means of creating jobs and stimulating the economy.

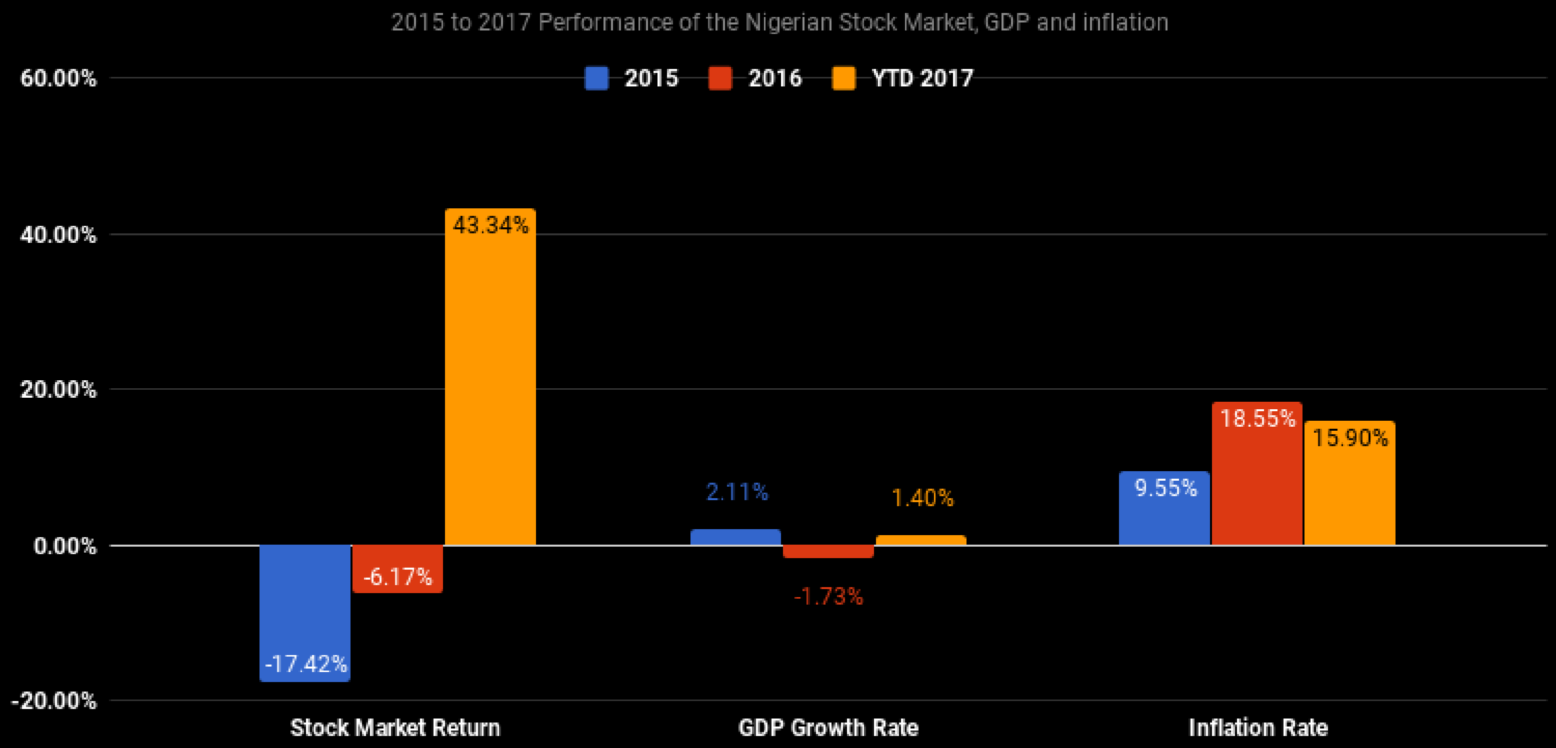
As borrowing increases to fund budget deficits, the country's servicing costs as a percentage of GDP will rise to up to 24.1 percent of GDP by 2018, according to the IMF—Nigeria's debt-to-GDP ratio was 18.6 percent in 2016, and 12.1 percent in 2015. Foreign borrowing in particular, will increase the economy's vulnerability to exchange rate depreciation. Nonetheless, Nigeria is expected to sustain economic growth in 2018.

The government's projections are, however, significantly more ambitious than those of independent bodies. The International Monetary Fund (IMF) predicts the economy will grow by 0.8 percent in 2017 and 1.9 in 2018. Fitch on 8 December cut its 2017 economic growth forecast to 1 percent, down from 1.5 percent because of the fragility of Nigeria's economic recovery. The World Bank in October cut its 2017 growth forecast to 1 percent from 1.2 percent due to lower than anticipated oil production and subdued non-oil sector growth.

FINANCIAL MARKETS

A TURNAROUND YEAR?

As a highly import dependent economy with a significant percentage of its earnings realized from the export of crude oil, improvements in Nigeria's foreign exchange reserves, increasing confidence and capital inflow into the economy, and improvement in the price of crude oil in the international market were some of the factors that fueled the 2017 recovery. In addition, the policies of the Nigerian Federal Government geared towards economic growth and recovery and independence in petroleum refining contributed a great deal to the improvement.



*Data as of December 22, 2017

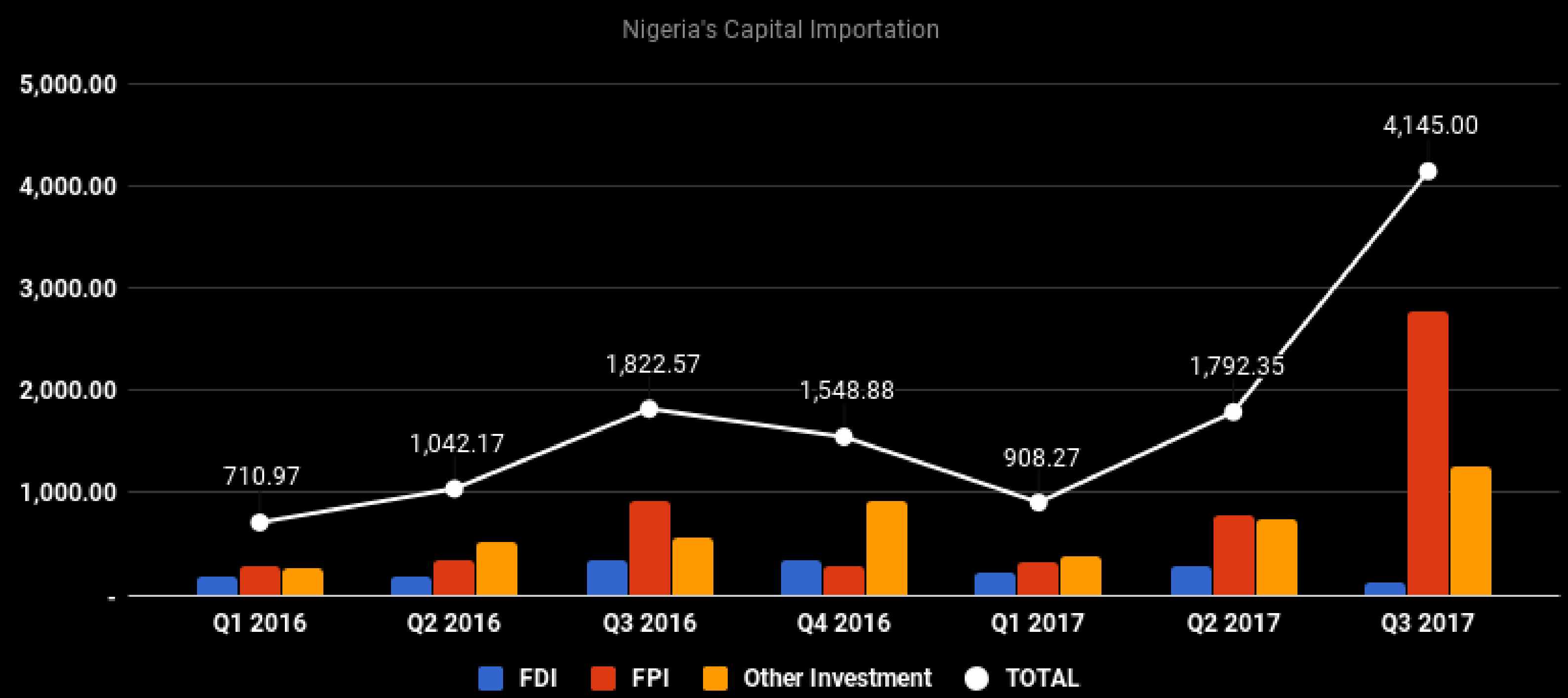
IMPROVEMENT IN CAPITAL INFLOWS AND CURRENCY OUTLOOK

Foreign Capital inflows into the country improved tremendously in 2017 with total 2017 capital importation up to the third quarter (Q3) of 2017, at US$6,845.62 million, already 34% higher than the total capital imported in 2016. In addition, compared to 2016 when Other Investment (mainly in the form of loans) contributed the largest share of 44% to total capital imported, Foreign Portfolio Investment (FPI) contributed the largest share of 56% in 2017.

This trend followed improvement in the economic outlook of the country, the accretion to its foreign exchange reserves, and the improvements observed in the Investors and Exporters (I&E) foreign exchange window set up by the Central bank of Nigeria (CBN) in April 2017, which all boosted investors' confidence in the Nigerian markets.

*Data as of December 22, 2017

IMPROVEMENT IN CAPITAL INFLOWS AND CURRENCY OUTLOOK

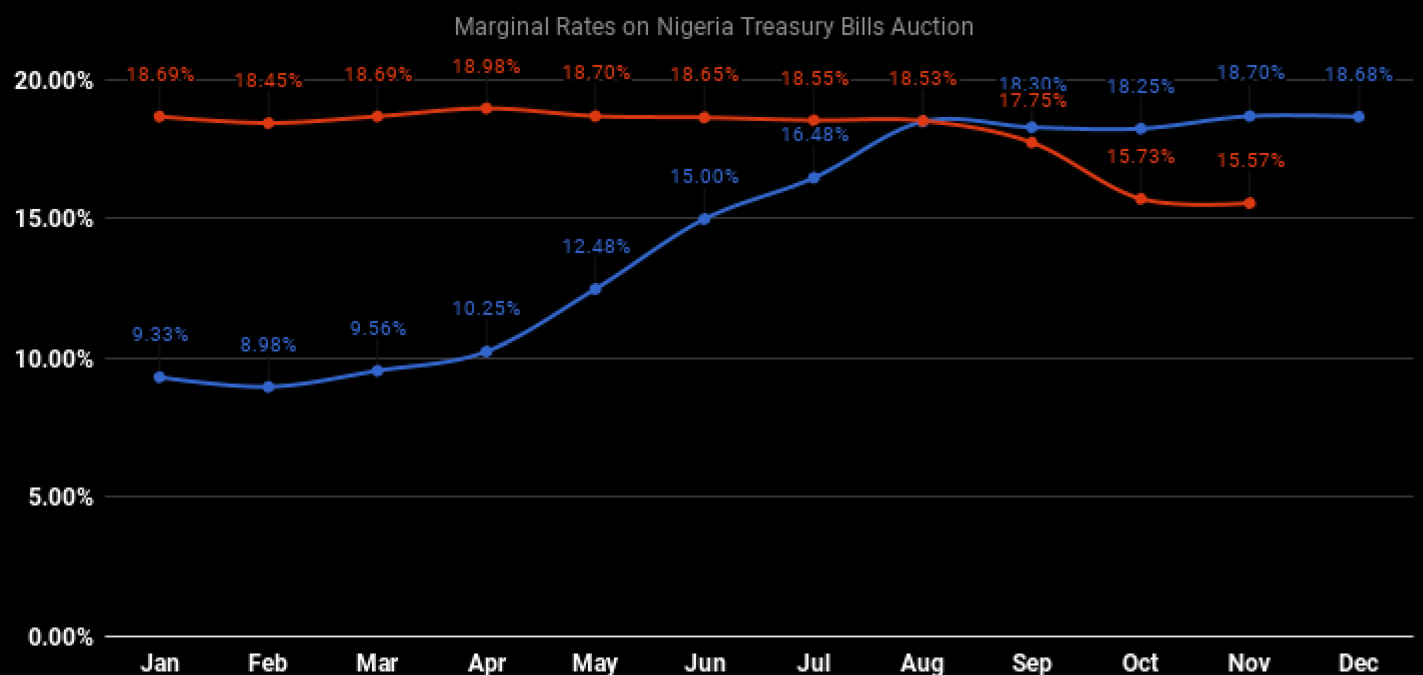


Breaking down the 2017 year-to-date FPI figure (US$3,851.42 million), data obtained from The Nigerian Stock Exchange revealed that total foreign capital inflow into Nigerian equities for the year 2017 (up to September 2017) was N468.30 billion (US$1,530.94 million), about 40% of the total YTD 2017 FPI figure, indicating that the balance of 60% flowed into fixed income instruments (this assumed that the total foreign inflow into equities was new capital and not reinvestment of capital already in the economy). The flow into equities in 2017 was an 83% increase over the 2016 equity inflow of N256.52 billion (US$840.44 million). In addition, YTD 2017 net capital flow into equities was positive N153.26 billion (US$501.03 million) as against a net outflow of N4.51 billion (negative US$14.78 million) in 2016.

*Data as of December 22, 2017

PERFORMANCE OF FIXED INCOME & BOND MARKETS

Activities in the fixed income and bond markets were significantly larger than in equities in 2017 as revealed by the analyses above. This was largely due to the high yields and coupon rates seen in the markets in most parts of the year. In a bid to stem the outflow of capital from the economy in light of the recession that crippled the Nigerian economy up to Q1 2017 and the dwindling foreign exchange reserves, the fiscal and monetary authorities kept interest rates in the economy and coupon rates on Nigeria's sovereign bonds and Treasury Bills significantly high. This contributed to the lull observed in the Nigerian equities market up to mid Q2 2017.



*Data as of December 22, 2017

PERFORMANCE OF THE NIGERIAN EQUITY MARKET

*Data as of December 22, 2017

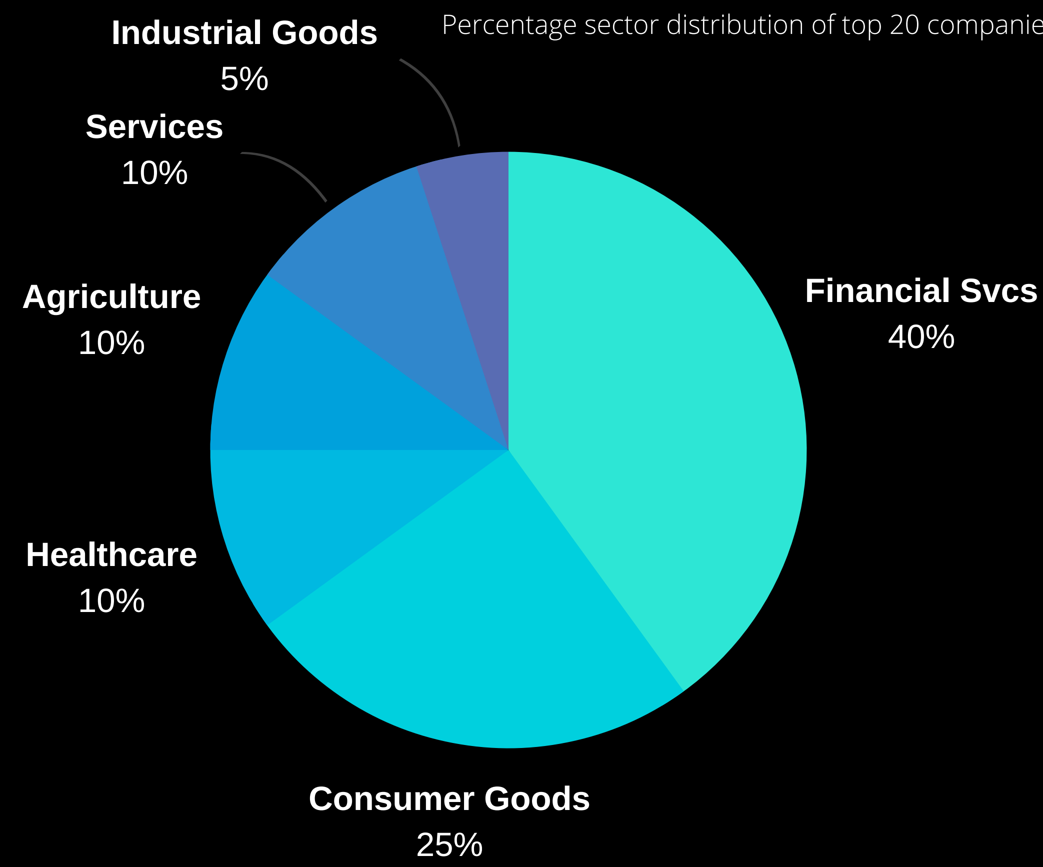
As at 22nd December 2017, the YTD return of All Share Index of The Nigerian Stock Exchange was 43.34%, as against -6.17% and -17.42% in 2016 and 2015 respectively. This was in line with the improving metrics and increased capital flow into the economy. As the economy recovered, the performances of many of the listed companies improved significantly, leading to increases in their share prices. The performance of the prices of the top 20 gainers ranged from 70.1% to 221.4% relative to the performance of the top 20 losers which ranged from -67.9% to -14.2%.

TOP GAINING/LOSING SECTORS

Relative to the negative performance observed in 2016 due to huge exposures to the oil & gas and other sectors of the economy, the performance of the companies in the Financial Services sector returned to positive in 2017 as many of the companies switched their investments into high yielding government bonds and treasury bills.

While the performance of some consumer goods and industrial goods companies turned positive with the recovery of the economy and availability of foreign exchange to procure essential inputs, the recovery of others were yet to be seen as they remain weighed down, probably by the policy of the CBN that banned the use of FOREX for the importation of some items.

Percentage sector distribution of top 20 companies



*Data as of December 22, 2017

Activities in the Healthcare, Services and Agriculture sectors continue to improve due to government support for increasing local content, import substitution and export promotion drives, partnerships with foreign counterparts and the recovery of the economy.

TOP GAINING/LOSING COMPANIES

TOP GAINERS	SECTORS	%Δ IN PRICE	TOP LOSERS	SECTORS	%Δ IN PRICE
Dangote Sugar Refinery	Consumer Goods	221.4%	Morison Industries	Healthcare	-67.9%
International Breweries	Consumer Goods	191.9%	Forte Oil	Oil and Gas	-48.5%
Fidson Healthcare	Healthcare	189.1%	University Press	Services	-46.2%
Fidelity Bank	Financial Services	183.3%	Mobil Oil Nig	Oil and Gas	-39.1%
Dangote Flour Mills	Consumer Goods	182.6%	MRS Oil Nigeria	Oil and Gas	-36.5%
May & Baker Nigeria	Healthcare	180.9%	Smart Products Nig.	Construction/Real Estate	-28.9%
Stanbic IBTC Holdings	Financial Services	176.7%	Julius Berger Nig.	Construction/Real Estate	-27.4%
FBN Holdings	Financial Services	168.7%	A.G. Leventis Nig.	Conglomerates	-27.1%
C & I Leasing	Services	164.0%	Total Nigeria	Oil and Gas	-26.8%
Airline Serv. & Logistics	Services	138.0%	NCR (Nigeria)	ICT	-26.1%
United Bank for Africa	Financial Services	128.9%	Conoil	Oil and Gas	-25.3%
NASCON Allied Ind.	Consumer Goods	115.8%	Trans-Nationwide Expr.	Services	-25.0%
Cement Co. of North.Nig.	Industrial Goods	90.0%	John Holt	Conglomerates	-24.2%
Nestle Nigeria	Consumer Goods	82.1%	Tripple Gee and Co.	ICT	-22.1%
PRESCO	Agriculture	79.6%	7-Up Bottling Comp.	Consumer Goods	-21.0%
Access Bank	Financial Services	78.9%	Nigerian Enamelware	Consumer Goods	-20.8%
Okomu Oil Palm	Agriculture	77.4%	Meyer	Industrial Goods	-19.5%
Zenith Int'l Bank	Financial Services	72.9%	Champion Brew.	Consumer Goods	-18.0%
Diamond Bank	Financial Services	70.5%	AIICO Insurance	Financial Services	-15.9%
Ecobank Transnat'l Inc.	Financial Services	70.1%	Union Dicon Salt	Consumer Goods	-14.2%

Top 20 Gaining and Losing Companies for 2017 (*Data as of December 22, 2017)

Given the extension of the supply cut of the Organization of the Petroleum Exporting Countries (OPEC) to the end of 2018, the improvement in the price of crude oil is expected to be sustained, thus leading to increasing foreign exchange earnings and reserves for Nigeria as well as a likely appreciation of the Naira. Investors' confidence in Nigerian markets is also expected to improve significantly and lead to the inflow of foreign capital majorly in the forms of Foreign Portfolio Investments and Other Investments.

However, the activities of the shale oil producers of the US may jeopardize the expected outcome of the OPEC led cuts and increase crude oil supply. In addition, the pace of increase of interest rate by the US Federal Reserves and the upcoming 2019 elections in Nigeria may affect capital inflow into the economy.

2018 FINANCIAL MARKETS OUTLOOK (CONTD.)

The continued decrease in Nigeria's inflation rate which began in February 2017 will undoubtedly give the CBN more leeway to reduce interest rates. In addition, the resolve of the fiscal authorities to substitute local bonds (with high yields and coupon rates) with foreign ones will bring down the high rates observed in the Treasury Bills and Sovereign Bond markets. Thus, unlike the trend observed in 2017, the stock market may benefit more from the expected inflow of foreign capital than the fixed income markets in 2018 as investors switch to the stock market in search of higher returns.

However, the improvements seen in the inflation rate may reduce in the coming year given that the food inflation rate has been trending upwards and has remained slightly above 20% for five consecutive months, unlike the core inflation rate which stood at 12.21% as at November 2017. If food inflation remained high in 2018, the CBN may be limited in its move to bring down interest rates, thus keeping yields and coupons in the fixed income markets high. Nevertheless, the impact of the substitution of local bonds with foreign bonds, which is already being implemented, in pushing down interest rates is expected to be greater.

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