MERISTEM

Macro and Market Insight

March 2023

Macros

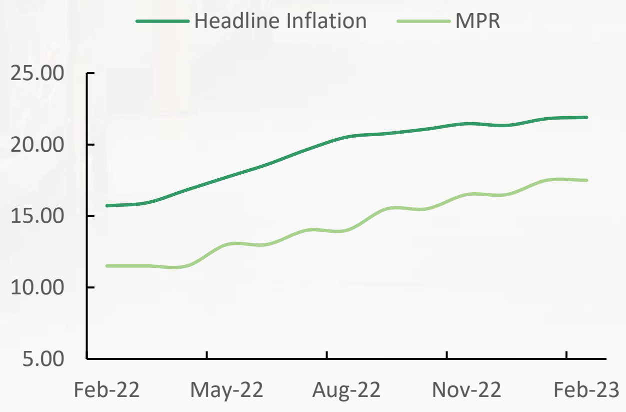
Macroeconomic Factors remain in Dire Straits…

Review

The first quarter of 2023 was quite eventful, as several macroeconomic events took place. The National Bureau of statistics reported a continuous uptick in the inflation rate, pitching at 21.91% YoY as of February 2023 (vs. 21.82% YoY in January 2023) and representing a 17-year high. Familiar factors continue to drive this northward movement including persisting structural challenges in the agricultural sector, FX illiquidity, higher prices of liquid fuel.

However, we observe that month on month inflation moderated in February 2023 which can be attributed to the impact of cash crunch in the period. This led to lower demand for goods, as a significant part of transactions in the informal sector of the domestic economy is through cash. While the core index recorded its first disinflation in 11 months (due to a high base effect and lower international gas prices), **we identify the likelihood of the fuel subsidy removal by the incoming administration as an upside risk to core inflation in the medium term.**

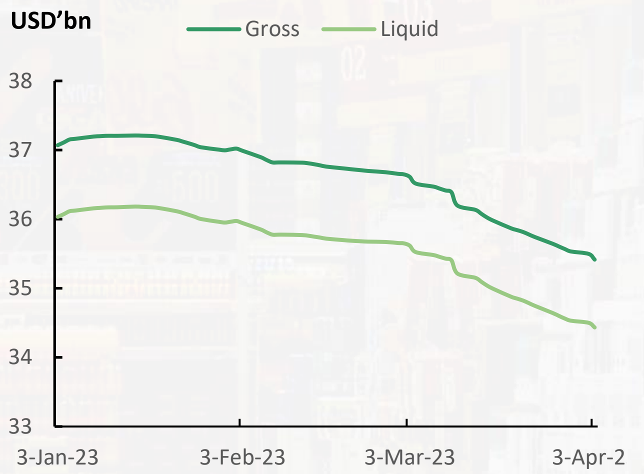
Chart 1: Headline Inflation and MPR (%)



Source: NBS, CBN, Meristem Research

In response to the increasing inflation numbers, the monetary policy authority sustained its aggressive stance, raising the Monetary Policy Rate (MPR) by a quarterly cumulative of 150bps to 18.00% while keeping other parameters constant. In line with our expectations at the beginning of the year, we note the general tone of the committee communicating a potential dovish tilt.

Chart 2: External reserve balance (Jan – March 2023)



Source: CBN, Meristem Research

The external reserve balance also continued to decline all through the first quarter, shedding USD1.67bn as the high petroleum subsidy bill and low accretion from non-oil sources have continue to deplete the reserves. The apex bank's interventions in the inter-bank foreign exchange market aimed at enhancing supply also pulls the balance further downward. **We express concern on this continuous free fall given that no major inflows (asides oil receipts) are certain to improve the reserve balance before the expected Eurobond maturity of USD500mn in July 2023**.

On the fiscal side, concerns surrounding the country's mounting debt burden sustained in 2022FY as the Debt Management Office (DMO) reported that the FGN total public debt increased by 16.92% to NGN46.45trn. Another controversial aspect of Nigeria's public debt is the financing of the FGN source from the CBN, popularly called "Ways and Means" (W&M). The additional borrowing from W&M in 2022 alone was NGN6.32trn (Jan-Oct 2022), which represents c. 105% of 2021 FGN revenue and c. 86% of the total 2022 FGN budget deficit.

Macros

...Yet, a Glimmer of Optimism

A positive surprise was however recorded in the Gross Domestic Product report released by the NBS for Q4:2022 as output grew by 3.52% in the quarter (3.10% in 2022FY). The non-oil sector remained the primary driver of output growth with a growth rate of 4.84% YoY. On a sub-sector basis, the information and communication (9.76% YoY), trade (5.13% YoY), financial services (16.36% YoY), and agriculture (1.88% YoY) sectors were the main drivers of this growth as the oil sector remained in contraction (19.22%YoY).

Still on a positive note, Nigeria recorded a trade surplus for the first time since 2019, mainly driven by the increase in crude oil prices and reduced pace of imports growth. **We opine that the prevalent challenges with FX sourcing impacted manufacturers ability to import required raw materials. In our view, the current increase in crude oil prices and observed increased in production volume portends positives for the trade balance. Thus we expect the trade surplus to sustain if these conditions persist.**

Key expectations for April 2023

- ***In the near term, we expect a moderation in inflation hinged on the expectation of a moderation in food inflation. This is due to a high base impact and slower demand for food products brought on by the economic cash crunch.***
- ***On the monetary side, we envisage an additional 50bps rate hike in the second quarter of the year .***
- ***Given the improved oil production performance and the expectation of higher oil prices (driven by the Organization of Oil Exporting Countries (OPEC) production cuts) we project an improvement in the oil sector GDP and trade balance.***
- ***For the non-oil sector, we foresee a slow down in growth due to the cumulative effect of higher interest rates, which is anticipated to raise borrowing costs. Overall, We anticipate output growth to remain positive, but slower than last year.***
- ***Finally, we assert that the economy will benefit from the increase in oil output volumes. As it is expected to result in higher revenue and foreign reserve improvement, which has been on a downward trend.***

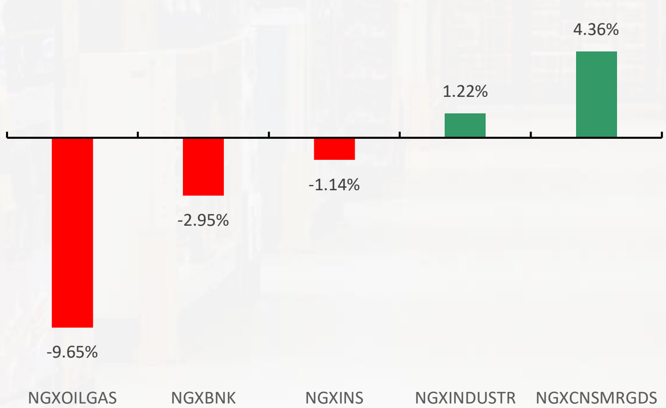
Equities

Local Bourse Remains Positive

Review

For the first time in five months, the local bourse recorded a monthly decline in March as the All-Share Index shed 2.82% MoM to settle at 54,232.34 points. Also, market breadth for the month declined to 0.63x (falling below the 1.00x mark for the first time since October 2022). This reflected the broadly bearish sentiment in the market. Across sectors, two indices - Consumer Goods (+4.36% MoM) and Industrial Goods (+1.22% MoM) recorded gains, while the Banking (-2.95% MoM), Oil and Gas (-9.65% MoM) and Insurance sector (-1.14% MoM) indices all lost. We attribute the bearish performance to investors taking profit on stocks that have gained in the prior months.

Chart 3: **Sectoral Performance**



Source: *Bloomberg, Meristem Research*

Assessing the first quarter as a whole however, the market returned 5.82% in line with our expectations for the quarter. Also, domestic investors participation in the market remained strong, as the volume of stocks traded and market turnover were 50.87% and 40.58% higher than the previous quarter.

A Flurry of Earnings Releases: The month was marked with a flurry of earnings releases. Performance across board was broadly positive, with equally attractive dividend declarations. Particularly, banks' results were highly anticipated, due to uncertainties around the impact of the Ghana's sovereign debt restructuring on their books, as well as general scepticism following multiple banks collapses globally.

Heavyweights Take a Beating

Another major contributor to the loss recorded in the market is selloffs on heavy weight stocks. Particularly, the 11 of the 15 most capitalised stocks on the exchange cumulatively shed 3.49% MoM.

Table 1: **Monthly Return of Selected Large Cap Stocks**

Ticker	Loss	% Market Cap
AIRTELAFRI	-8.70%	18.75%
MTNN	-2.04%	16.48%
DANGCEM	-2.88%	15.52%
BUACEMENT	-1.61%	11.18%
ZENITHBANK	-2.45%	2.74%
GTCO	-4.32%	2.53%
SEPLAT	-13.21%	2.28%
STANBIC	-9.83%	1.64%
FBNH	-4.72%	1.34%
NB	-10.52%	1.25%
ACCESSCORP	-5.76%	1.08%
		74.79%

Source: *Bloomberg, Meristem Research*

During the month, **SEPLAT** announced that the company was served with a court order restraining its CEO from participating in the running of the company for seven days. The petition was following allegations of unfair, prejudicial and offensive acts, which the company refuted. Also, **SEPLAT** announced the termination of the consultancy agreement between the company's wholly owned subsidiary and its co-founder - Dr. A.B.C Ojiako. The termination was due to persistent material breaches notwithstanding a prior suspension of the consultancy agreement in February. The led the stock to lose 13.21% during the month contributed to the 9.65% MoM loss on the Oil and Gas sector index given its status as an heavyweight ticker.

OANDO Plc announced that the company's majority shareholder Ocean and Oil Development Partners Limited (**OODP**) has made a bid to buy out all minority shareholders in the company. We made our recommendation on the transaction HERE.

ZENITHBANK also revealed that the CBN granted it Approval-In-Principle to operate a non-operating Financial Holding Company structure. Upon formation, **ZENITHBANK** will consolidate its various subsidiaries into one.

Equities

Key Expectations for April

With the recent decline in price, especially on heavy weight tickers, we expect investors to cherry pick on attractive tickers this month. Also, we anticipate that the hunt for dividends will spur buying interest on high dividend paying stocks ahead of closure of register. Finally, we expect dividend markdown to also present attractive buying opportunities for investors looking to enter the market. Thus, we expect the mood in the market to be broadly positive this month.

We recommend that investors take advantage of the dividend season to accumulate stocks with attractive dividend yields. Kindly see our dividend 2022FY dividend portfolio below:

Final Dividend Yield										
Ticker	2018	2019	2020	2021	Average	2022e	CP	TP	Upside %	Closure Date
ACCESSCORP	3.68%	4.00%	6.75%	7.53%	5.49%	9.90%	9.00	11.12	23.56%	TBA
AFRIPRUD	12.92%	17.50%	8.00%	7.87%	11.57%	8.26%	6.05	8.12	34.21%	21-Apr-23
FIDELITYBK	5.42%	9.76%	8.73%	13.73%	9.41%	8.16%	5.36	5.61	4.66%	TBA
MAYBAKER	8.16%	12.95%	8.55%	7.46%	9.28%	5.90%	4.50	5.03	11.78%	TBA
TOTAL	6.90%	6.05%	4.68%	8.20%	6.46%	9.60%	218.80	237.70	8.64%	28-Apr-23
UBA	8.44%	11.19%	4.05%	9.94%	8.40%	10.71%	8.40	9.43	12.26%	17-Apr-23
ZENITHBANK	10.85%	13.44%	10.89%	11.13%	11.58%	11.24%	25.80	26.69	9.92%	17-Apr-23

**prices are updated as at April 3rd 2023*

Please click the link attached to view the full report.

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Fixed Income

System Liquidity Calls The Shot

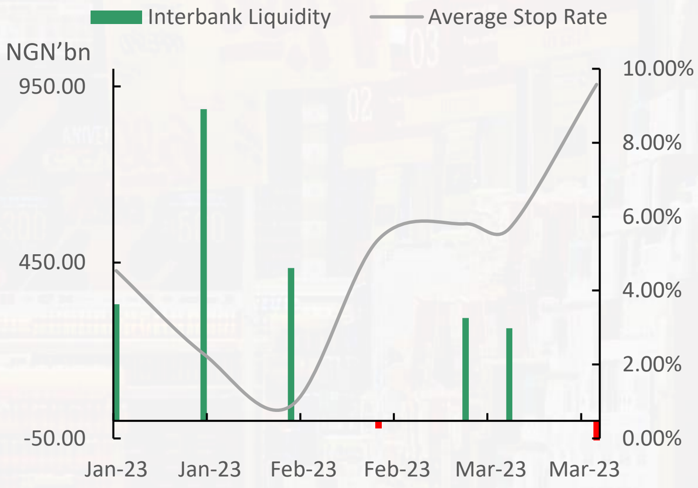
Review

Following previous trends, three Treasury Bills' Primary Market Auctions (PMA) were held in March to mark the end of the first quarter. Across the three PMAs, a total value of NGN631.84bn was allotted out of the total subscription of NGN2.11trn. However, the last PMA in Q1:2023 took a different dynamic relative to the previous auctions held in 2023. For the first time in 2023, the auction's average stop rate (9.58%) surpassed 9.00%. Although this was unsurprising as the system liquidity at the auction date (March 29) plunged to a negative value of NGN522.43bn. Hence, the auction was characterized by lower investors' demand, demonstrated by the lowest bid-to-cover ratio (1.16x) recorded in March. Expressly, stop rates on the 91-Day, 182-Day, and 364-Day instruments jumped significantly by 345bps, 300bps, and 525bps to 6.00%, 8.00%, and 14.74%, respectively.

At the Bond auction, investors' demand for the instruments increased, as evinced by the higher bid-to-cover ratio (1.44x vs 1.29x at the previous auction). Subsequently, the marginal rates of Apr-2032, Apr-2037 and Apr-2049 bonds declined by 15bps, 70bps, and 25bps to 14.75%, 15.20% and 15.75%, respectively, while that of Feb-2028 increased negligibly by 1bps to 14.00%.

At the secondary market, the mood was predominantly bearish as investors sold off some of their positions due to the relatively tight system liquidity. Consequently, the average T-bills and bond yields rose to 7.95% and 13.56% at the end of March (vs 4.94% and 13.27% at the end of February), respectively.

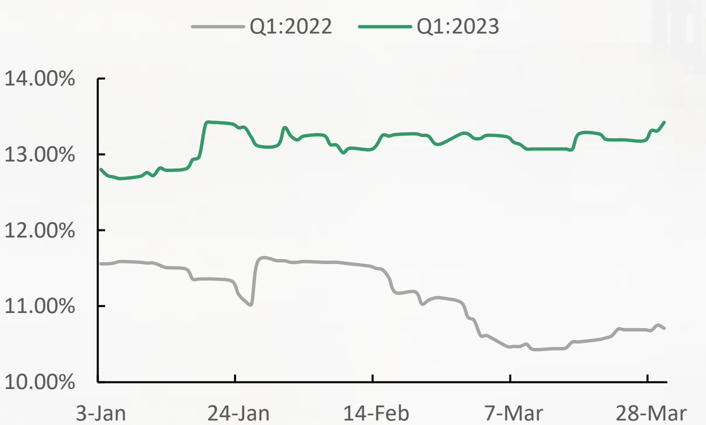
Chart 4: **Liquidity and Stop Rates at the T-bills PMA**



Source: *CBN, Meristem Research*

Comparing the fixed-income market dynamics of Q1:2023 and its corresponding period in 2022 revealed a similar trajectory of yields. For both periods, the influx of liquidity significantly impacted the direction and suppressed yields.

Chart 5: **Average Bond Yield in Q1:2022 and Q1:2023**



Source: *FMDQ, Meristem Research*

Fixed Income

In the Eurobond market, there were notable selloffs on the instruments, which took the average yield to a month-high of 11.00%. This can be attributed to the global banking crisis experienced during the month as well as the additional 50bps MPR hike. However, increased buying activities at the end of the month moderated the average Eurobond yield to 9.80%. Nonetheless, the yield stayed higher relative to 9.74% at the end of February.

In addition, commercial paper issuances increased as corporates looked to raise funds from the local debt market, mainly for refinancing and working capital needs. Thus, the issuers offered yields ranging between c. 11% and c. 23%.

Key Expectations for April

This month, we foresee a decline in both T-bills and Bond yields. On the demand side, the Government has indicated its intention to raise a total of NGN641.00bn (NGN281.10bn T-bills, NGN360.00bn bonds). On the supply end, the maturity of the Apr-2023 FGN Bond (NGN735.96bn), inflows from coupon payments (NGN342.57bn), and T-bills maturities (NGN281.10bn) are anticipated to hit the market. Therefore, we expect robust system liquidity to suppress yields in the fixed-income market. Thus, we recommend that investors take a long position, as this presents an opportunity for capital appreciation in line with our expectation of lower yields.

For the Eurobond instruments, the country's deteriorating macroeconomic conditions could cause investors to reprice and demand higher yields.

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