MERISTEM

Macro and Market Insight

January 2024

Macros

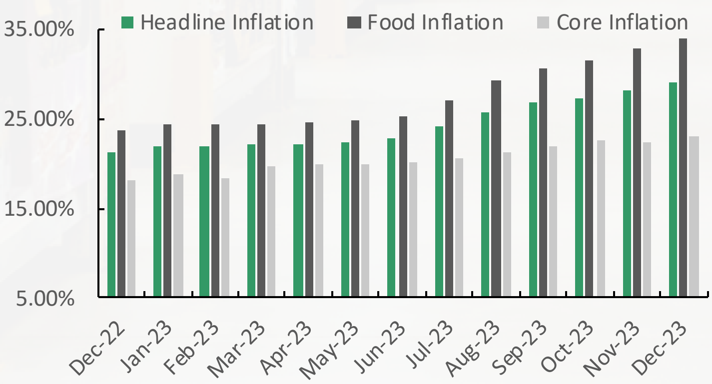
Deteriorating Indicators, Proactive Policies for Growth

Review

In January, several key developments influenced the macroeconomic landscape of the country. These include persistent challenges in Nigeria's foreign exchange market, a surge in inflation rate, and the Federal Government's initiatives aimed at providing support to enhance the country's outlook.

The National Bureau of Statistics (NBS) reported that Nigeria's headline inflation continued to rise for the twelfth consecutive month to 28.92% YoY and 2.92% MoM in December 2023, up from 28.20% YoY and 2.09% MoM in November 2023. Elevated food prices caused by persistent supply constraints in the country's agricultural value chain, a heightened demand for food items during the festive season, and higher transport costs led to this rise. As a result, food inflation rose to 33.93% YoY (vs 32.84% in November 2023 and 23.75% in December 2022). Similarly, the core index rose to 23.06% YoY (vs. 22.38% in November 2023 and 18.21% in December 2022) on the back of a further depreciation in the Naira and increased festivities spending on clothes, pharmaceuticals, restaurants and hotel costs, amongst others.

Chart 1: Trend in Headline, Food, and Core Inflation (% YoY)



Source: NBS, Meristem Research

In the near term, we expect inflation to remain on the uptrend hinged on:

➢ Continued limitations in the production of food in various regions and an increase in transportation and logistics expenses leading to an uptick in food prices.

➢Expected depreciation of the country's currency's which could increase core and imported inflation.

➢ Expected increases in energy costs, partly due to OPEC+ supply cuts and a likely hike in electricity tariffs in 2024.

The Central Bank of Nigeria (CBN) revealed that inflationary pressure in the country is anticipated to decline in 2024 with CBN's inflation-targeting policy, which aims to curb inflation to 21.40% at the end of the year. The decline is expected to be driven by enhanced agricultural output and alleviated global supply chain constraints.

We opine that while increased agricultural output may contribute to slowing inflation and a high base effect could moderate inflation figures (especially in the latter half of the year), reaching this target range in 2024 is unlikely as persistent factors such as the depreciation of the naira and rising transportation costs continue to drive inflation in the country.

In a recent development, the Central Bank of Nigeria (CBN) has issued a directive, placing strict limits on the Net Open Position (NOP) of Nigerian banks concerning their exposure to foreign currencies. According to this directive, banks must adhere to a maximum NOP of 20% short position or 0% long position of shareholder's funds unimpaired by losses.

We believe this initiative reflects the CBN's efforts to restore balance to the FX market and regulate the country's exchange rate volatility. Moreover, we anticipate that the directive may prompt a short-term appreciation of the Naira as banks move to comply and realign their foreign currency assets and liabilities. This adjustment could also foster improvements in banks' risk management strategies, ensuring adequate capital reserves to mitigate potential losses. However, we note that the impact on the FX market may be transitory, given the persisting challenges of low FX supply and market illiquidity, which could potentially limit the directive's long-term effectiveness.

Seven major oil marketers, including Conoil Plc, Ardova Plc, 11 Plc, MRS Oil Nigeria Plc, OVH Energy Marketing Ltd, Total Energies Plc, and NNPC Retail, have entered a partnership with the Dangote Petroleum Refinery for the distribution of refined petroleum products. This collaboration follows the initiation of oil production by the Dangote Refinery earlier in January, commencing with diesel and aviation fuel after the receipt of six million barrels of crude oil from the Nigerian National Petroleum Corporation (NNPC).

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We anticipate that this arrangement will reduce the country's reliance on import for refined crude products and contribute to a decline in landing and logistic costs for downstream players in the industry.

Additionally, the Nigeria Export-Import Bank unveiled a digital hub called 'Cocoa Connect Africa' as part of its efforts to enhance cocoa production in the country. This initiative aims to centralize all cocoa industry stakeholders' activities onto a single platform, facilitating connections between producers and potential buyers. Additionally, it will serve as a hub for market information and networking, bringing together participants across the cocoa value chain.

We anticipate that this platform will expand the cocoa market's reach, enhance industry efficiency and growth prospects for the industry especially with the price of cocoa on the rise.

Elsewhere, the Federal Government of Nigeria has disclosed plans to partner with Luan Steel Holding Group, a Chinese firm, to establish a functional steel industry and initiate military hardware production at the Ajaokuta Steel Plant. This initiative underscores the government's goal of advancing industrialization and maximizing the steel industry's potential to drive economic growth. Additionally, this initiative could serve as a channel for inflows into the country in the form of foreign direct investments, create job opportunities, and contribute to the ongoing efforts of the federal government to combat insecurity and terrorism in the country.

We opine that if successfully executed, this endeavor has the potential to rejuvenate the steel industry, enhance security, and ultimately enhance economic growth.

In line with the government's objective of poverty alleviation, the Federal Government of Nigeria has allocated NGN150bn to implement poverty alleviation programs in 2024 under the National Poverty Reduction and Growth Strategy. The fund is to be spent under four pillars which are macroeconomic stability, industrialization, structural policies/institutional reforms, and redistributive policies/programs of the government. The program is expected to run for ten years (2021-2031), with an estimated implementation cost of USD1.60trn. This is a positive development, as it is expected to alleviate the cost-of-living challenges and provide relief to the hardships faced by the population in line with the federal government's policy reforms.

Key Expectations for February 2024

- ***Sustained upward trajectory in headline inflation.***
- ***Further weakening of the Naira against the dollar due to FX illiquidity.***
- ***Enhanced economic growth premised on improved oil output and better performance of the non-oil sector.***
- ***A 50 to 100 basis point hike in the Monetary Policy Rate (MPR) at the upcoming monetary policy committee meeting as inflation continues northward.***

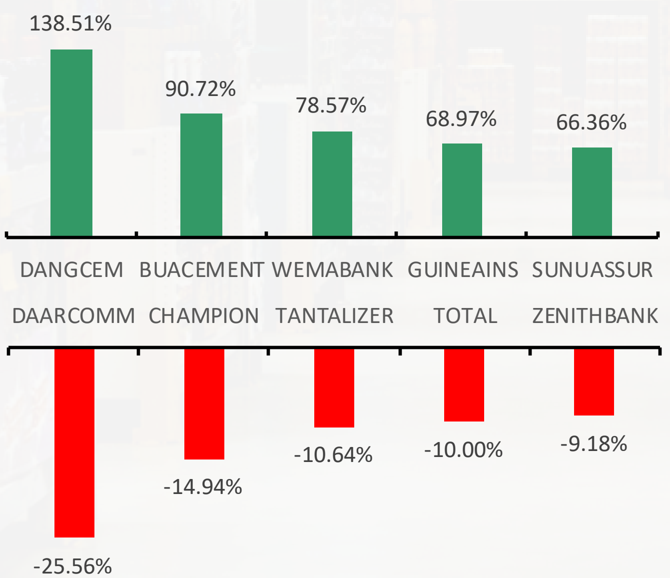
Equities

An Unprecedented Strong Start: The Bulls Charge Ahead

Review

In an unprecedented start to the year, the Nigerian equities market gained **35.28%** MoM in January 2024, marking the highest monthly return since May 2009. Notably, the All-Share Index (**NGX-ASI**) surpassed the 100,000pts mark to reach a peak of 101,154.50pts. Reflecting the upbeat mood, market breadth widened to 2.72x (vs 2.42x in December 2023) as 80 stocks recorded monthly gains while 32 stocks closed in the red zone. Similarly, trading activity levels more than doubled - value and volume traded increased by 93.10% and 132.30% to NGN324.23bn and 18.80bn units from NGN167.91bn and 8.09bn units in December 2023.

Chart 2: Top Gainers and Losers for January 2024

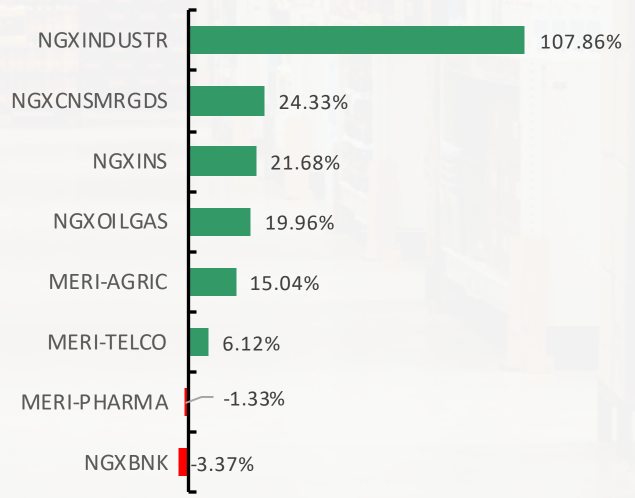


Source: Bloomberg, Meristem Research

(+90.72% MoM) reached record high prices of NGN763.00 and NGN185.00, respectively. Although the year began on a highly positive note for the banking sector, sentiments shifted at the tail end of the month. The Central Bank of Nigeria's (CBN) directive on the banks' Net Open Positions contributed to a subdued outlook and prompted profit-taking on banking stocks. Some tickers with losses include – **ZENITHBANK** (-9.18% MoM), **GTCO** (-8.64% MoM), **STANBIC** (-6.68% MoM), **FBNH** (-7.86% MoM) amongst others.

*N:B – **MERI-PHARMA** is our newly introduced index which tracks the performance of all healthcare stocks listed on the Nigerian Exchange (NGX).*

Chart 3: Monthly Sectoral Returns in January 2024



Source: Bloomberg, Meristem Research

Sectoral Performance: Industrials Goods take the Lead

Across sectors, five (5) out of eight (8) indices under our tracking closed in the green zone this month - **NGXINDUSTR** (+107.86% MoM), **NGXCNSMRGOODS** (+24.33% MoM) **NGXINS** (+21.68% MoM), **NGXOILGAS** (+19.96% MoM), **MERI-TELCO** (+6.12% MoM) and **MERI-AGRIC** (+15.04% MoM) while **NGXBNK** (-3.37% MoM) and **MERI-PHARMA** (-1.33% MoM) closed in the red zone. Notably, the industrial goods tickers were at the fore-front of activities owing to heavy buying interests as investors continued to accumulate. Consequently, **DANGCEM** (+138.51% MoM) and **BUACEMENT**

Bell-weather Tickers Change Spots

At the end of the month, the NGX market capitalisation advanced by 37.90% to NGN56.43trn (vs. NGN40.92trn in December 2023), thus underscoring the increased market activity during the month. Notably, we observed that **DANGCEM** became the most capitalised stock in the local bourse and the first listed company to cross over the NGN10.00trn market capitalization, reaching NGN13.00trn as of January 31, 2024. The reason for this rally is majorly attributed to buying interest from Mr. Femi Otedola, which spurred investor's optimism towards the ticker during the month.

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Equities

Table 1: Top Capitalised Stocks on the NGX (December 2023 vs January 2024)

Ticker	Market Cap. (Dec 2023) (NGN'trn)	Ticker	Market Cap. (Jan 2024) (NGN'trn)
AIRTELAFRI	7.09	**DANGCEM**	13.00
DANGCEM	5.45	**AIRTELAFRI**	7.52
MTNN	5.37	**BUACEMENT**	6.26
BUAFOODS	3.48	**MTNN**	5.72
BUACEMENT	3.28	**BUAFOODS**	4.89

Source: Bloomberg, Meristem Research

Notable Occurrences and Corporate Actions

Cadbury Nigeria Plc (**CADBURY**) stated its intention to issue additional share capital of 402,082,657 ordinary shares at 50 kobo each, increasing its total share capital by 21.41% to NGN1.14bn. This development stemmed from an outstanding debt of USD7.72mn (c. NGN7.04bn) owed to its parent company - Cadbury Schweppes Overseas Limited. In its resolution, the debt would be converted to additional shareholding in CADBURY. This brings the total shareholding of the parent company to 1,810,214,310, c.79% in CADBURY. As such, free float is expected to decline to 20.59% which is still within NGX's free float requirement. **The conversion of the total debt is anticipated to reduce the company's total debt balance and will positively impact the company's finance costs, ultimately enhancing its bottom line. However, we highlight the potential dilution effect to the company's existing shareholders and a likely reduction in earnings per share to NGN0.79 (from NGN0.95). Notwithstanding, we maintain our target price of NGN26.37 for 2024FY.**

Airtel Africa Plc (**AIRTELAFRI**) has disclosed its intention to launch a share-buy-back programme of about USD100mn (or its naira equivalent). Still awaiting regulatory approval, the programme is expected to begin in March 2024 and last over a 12-month timeline. This initiative aligns with the firm's positive long-term outlook and will be executed using its cash reserves as it has consistently maintained a positive operating cash position in recent years. **Nonetheless, we retain our SELL recommendation on the ticker as it is currently trading at NGN2,000 which is a 26.94% below our target price of NGN1,461.15.**

Furthermore, Access Holdings Plc (**ACCESSCORP**) announced that its banking subsidiary, Access Bank Plc, has taken action to acquire majority shareholding (c. 80%) in the Ugandan firm Finance Trust Bank Limited. Also, a notice by the Federal Competition and Consumer Protection Commission disclosed the acquisition of 81.82% of ARM Pension Managers (PFA) by Access Pension Limited, a subsidiary of Access Holdings. Following the acquisition, ARM Pension will merge with Access Pensions Limited, resulting in an entity with assets under management (AUM) surpassing NGN2.22trn. **In our assessment, the merger and acquisition is expected to enhance financial performance through expanded market share, increased revenue, and improved service offerings. The development also aligns with ACCESSCORP's strategy to expand across the African continent. As such, we expect this transaction to result in higher earnings and growth prospects for the company and increase investors' optimism towards their overall performance.**

Notore Chemical Industries (**NOTORE**), in a recent notice of an Extraordinary General Meeting, revealed its intention to raise additional capital of NGN105.79bn by issuing 2.42bn ordinary shares at NGN43.75 per share to a specific investor through a Private Placement, pending approval from relevant regulatory authorities. Furthermore, the company intends to raise the Share Capital from NGN2.00bn to NGN2.015bn by creating 30,165,500 ordinary shares at NGN0.50 each.

Summary of Key Expectations for February 2024

In February, we expect some factors to influence investors' sentiment to the equities market. Broadly, we anticipate a sustained positive momentum hinged on buying interest as investors react to earnings releases during the period and take advantage of tickers with attractive entry prices. However, occasional profit taking activities, particularly across sectors with lower-than-expected earnings performance. Also, we highlight that the expected uptrend in treasury yields during the period may sway investors' sentiment from the local bourse to the fixed income market.

Equities

As companies release their financial results for the fiscal year 2023, we recognize the significance of dividend investing for maximizing market opportunities. Considering this, we recommend the stocks listed below, emphasizing strong dividend yield and potential for capital appreciation.

Table 2: Stock Recommendation with Dividend Yield and Capital Appreciation

Ticker	Current Price (NGN)	Target Price (NGN)	Upside (%)	Expected Dividend Yield (%)
AFRIPRUD	8.05	9.54	18.51%	6.41%
CUSTODIAN	9.80	11.58	18.16%	6.32%
UCAP	23.00	28.39	23.43%	6.47%
ZENITHBANK	37.50	46.09	22.91%	8.03%

**Prices are updated as of February 6th, 2024*

Fixed Income

Treasury Yields Expected to Stay Higher

Review

In the opening month of 2024, the local debt market was marked by different activities including the conduct of three primary market auctions (two Treasury Bills and one Bond), amid ongoing efforts by the monetary authority to manage systemic liquidity through concurrent Open Market Operations (OMO) auctions.

At the T-bills auction, the Central Bank of Nigeria (CBN) offered a total sum of NGN288.38bn (vs. NGN184.95bn in December). While demand fell marginally, evinced by the total subscription (NGN1.11trn vs. NGN1.46trn in December 2023), the average bid-to-cover ratio increased to 12.42x from 4.05x in December 2023. This was due to the lower amount allotted in January (NGN288.38bn vs. NGN1.84trn in the previous month). Consequently, the average stop rate on the trio instruments fell to 6.46% vs. 10.86% in December 2023.

Similarly, at the FGN Bonds' Primary Market Auction (PMA) where the Debt Management Office (DMO) reopened four instruments – MAR 2027, APR 2029, JUN 2033, and JUN 2038, the total subscription fell by 31.80% MoM to NGN604.56bn from NGN886.41bn. However, the amount allotted was higher (NGN418.20bn vs. NGN273.63bn at the previous auction). Thus, the bid-to-cover ratio declined to 1.45x in January from 3.24x in December 2023. As a result, the DMO maintained the marginal rates across the offered instruments - MAR 2027, APR 2029, JUN 2033 and JUN 2038 at 15.00%, 15.50%, 16.00% and 16.50%, respectively.

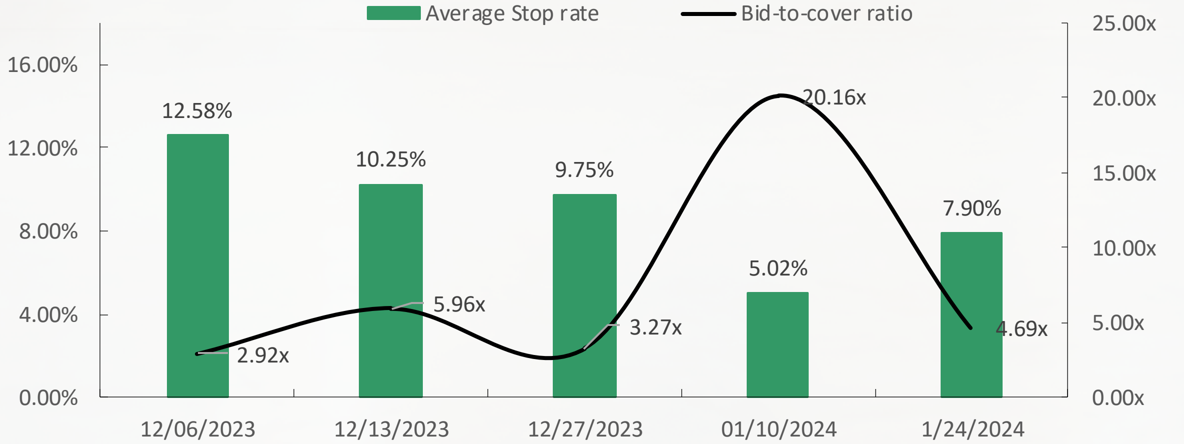
At the OMO auctions for the month, a total of NGN950.00bn was offered across three auctions. Despite the lower demand, evinced by the subscription to offer ratio (2.00x vs. 4.00x in December 2023), the CBN raised a total of NGN1.00bn across the three OMO auctions with the average stop rate at 13.50% (vs. 9.00% in December 2023).

The secondary market mirrored the activities of the primary market as mixed sentiment prevailed during the month. For context, the average T-bills yield fell to as low as 4.00% as of 12th January 2024, driven by robust system liquidity during the period. However, at the end of month, the average yield stood at 7.84% (vs 8.18% in December 2023). Conversely, the secondary market for bonds was bearish as the average bonds yield rose to 14.49% from 14.19% in December 2023.

Expectations for February 2024

Despite the Central Bank of Nigeria (CBN) issuing a directive to regulate Cash Reserve Ratio (CRR) debits, we anticipate that the proactive measures taken by the monetary authority in liquidity management will likely lead to an upswing in yields for both treasury bills and bonds. We also expect the high borrowing need of the government to drive greater demand, prompting investors to seek higher yields. Additionally, our outlook includes an expectation of a rate hike at the first Monetary Policy Committee (MPC) meeting of the year, leading to a potential narrowing of the negative real rate of return.

Chart 4: Average T-bills Stop Rate and Bid-to-Cover Ratio (December 2023 – January 2024)



Source: ***CBN, Meristem Research***

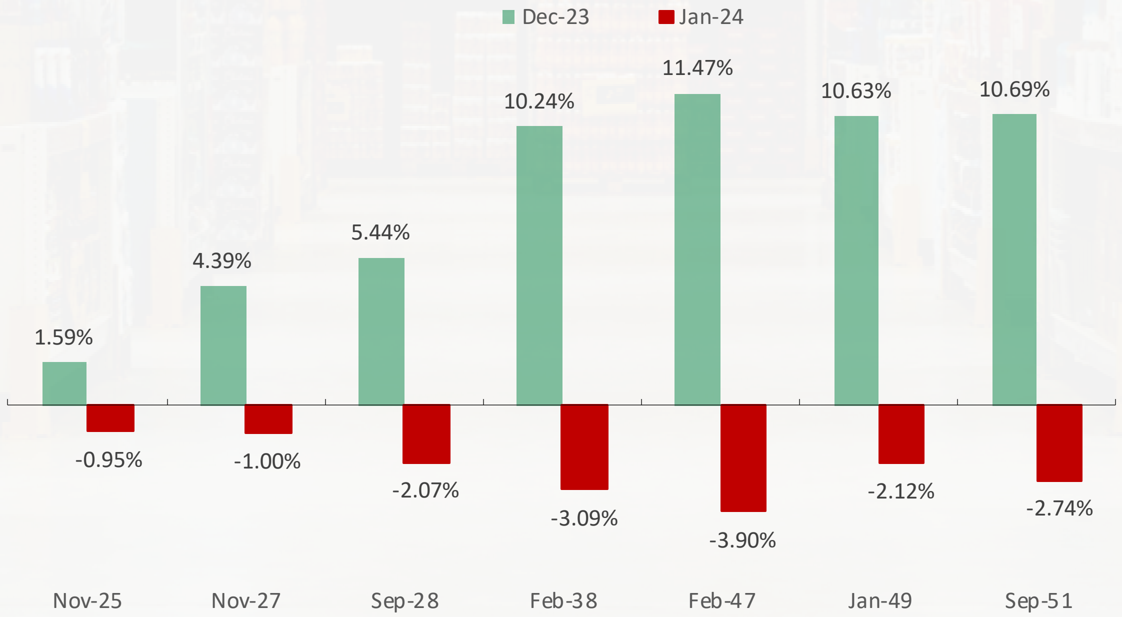
Fixed Income

In January, the sentiment in the Eurobonds market was generally mixed. Earlier in the month, we observed sell pressure across the curve which drove yields higher, particularly on the FEB-39 instrument. However, a bullish sentiment prevailed towards the end of the month, countering the bearish trend that persisted since the beginning of the year. This shift occurred as the CBN proactively addressed additional FX backlogs, attracting foreign portfolio investors who selectively chose instruments at appealing levels. Additionally, dampened expectations of rate hikes in major economies increased the attractiveness of SSA instruments during the period. Despite this positive shift, the average Eurobond yield increased to 9.86%, compared to the 9.38% recorded in December 2023.

Expectation for February 2024

In February, we anticipate a decrease in yields on Nigerian Eurobonds. This expectation is hinged on the sustained efforts of monetary authorities to address FX backlogs and the investors' positive perception regarding the direction of monetary policy.

Chart 5: Price Return on Selected Eurobond Instruments in January 2024 vs December 2023



***Source:* DMO, Meristem Research**

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