MERISTEM

Macro and Market Insight

Q1:2024

Macros

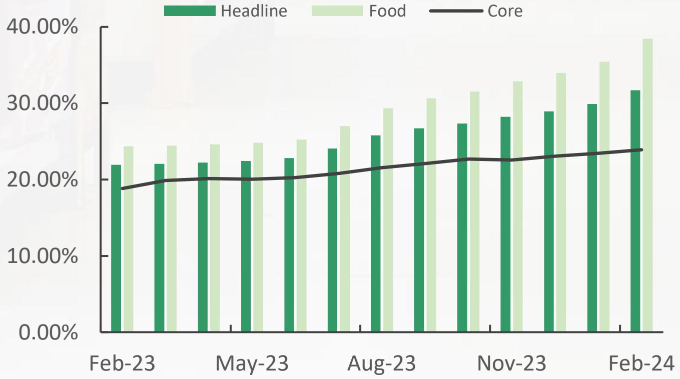
Deteriorating Indicators, Proactive Policies for Growth

Review

In Q1:2024, the macroeconomic landscape was influenced by several key developments. These include continued uptick in inflation, improved GDP and capital importation figures, the surge in the country's debt stock, the several interventions and policy reforms by the apex bank to stabilize the Naira and the resultant appreciation against the greenback.

Nigeria's headline inflation continued its upward trajectory, marking its 14th consecutive increase from 29.90% YoY in January 2024 to 31.70% YoY in February 2024 . Both the food and core indices recorded simultaneous upticks, reaching 37.92% YoY and 25.13% YoY (vs 35.41% and 23.59% in January 2024), respectively. This surge in annual food inflation was attributed to the continued strain in the country's food sector which led to higher prices of bread, cereals, tubers, oils, fish, and meat, among other staples during the period. Similarly, the core index increased due to increased prices of passenger transport, medical services, housing rentals, pharmaceutical products, and accommodation services. On a month-on-month basis, headline, food, and core inflation grew by 3.12%, 3.79% and 2.17%, respectively.

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



Source: NBS, Meristem Research

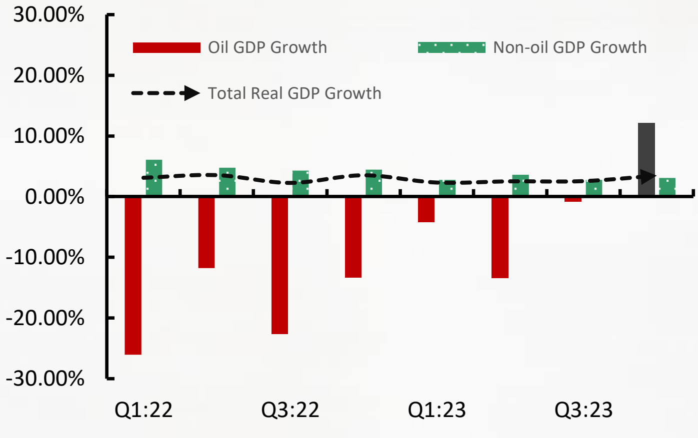
In the near term, we expect inflation to remain on the uptrend hinged on:

- **Continued limitations in the production of food in various regions due to insecurity and an increase in transportation and logistics expenses leading to an uptick in food prices.**
- **Anticipated mild appreciation in the country's currency which could lead to moderation in month-on-month core inflation and imported inflation.**

The Monetary Policy Committee (MPC) in an effort to maintain price stability have implemented two major hikes in the Monetary Policy Rates (MPR). In the February meeting, a 400 basis points (bps) increase bringing it to 22.75%, marking the highest hike rate pace in history. In its March meeting, another 200bps increase was implemented – taking the MPR to 24.75% (the highest level ever). Additionally, the Committee raised the Cash Reserve Ratio (CRR) by 1250bps to 45.00% for Deposit Money Banks while that of Merchant Banks was adjusted by 400bps from 10.00% to 14.00%. The Committee also adjusted the lower band of the asymmetric corridor to -700bps around the MPR (in its first meeting) and a reversal to -300bps in March, while keeping the liquidity ratio unchanged at 30%.

According to data from the National Bureau of Statistics (NBS), Nigeria's economy expanded by **3.46% YoY** in Q4:2023, compared to 3.52% in Q4:2022. This growth was primarily fueled by a significant recovery in the oil sector, which experienced a growth of **12.11% YoY**, marking a substantial improvement from the 13.38% YoY contraction recorded in Q4:2022 and ending 15 consecutive quarters of contraction. The growth in oil GDP can be attributed to higher oil production volumes, which averaged 1.53 million barrels per day (mbpd) in Q4:2023, up from 1.43mbpd in Q3:2023. Additionally, the non-oil sector grew by 3.07% YoY from 4.44% YoY in Q4:2022, driven by improved performance in sectors such as financial and insurance, ICT, agriculture, and trade, among others. Overall, the annual real GDP grew by **2.74% YoY** in 2023, down from 3.10% in 2022.

Chart 2: Real GDP YoY Growth (%)



Source: NBS, Meristem Research

Macros

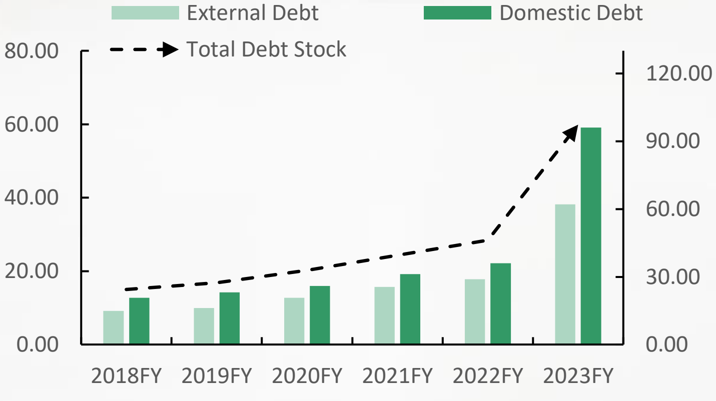
Looking ahead, we anticipate that the economy will sustain its growth trajectory, based on our projection of higher oil output (average of 1.55mbpd for 2024FY) on the back of various government initiatives aimed at boosting output in the sector. For the non-oil sector, our outlook remains modest. Anticipated improvement in the performance of specific sectors, including financial and insurance, coupled with the potential GDP basket rebasing during the year are factors supporting enhanced economic growth in 2024FY.

However, we anticipate continued pressure on the manufacturing sector, considering the MPC's cumulative 600bps hike in MPR in Q1:2024 and the subsequent constraints on production activities in the sector.

Thus, we review our 2024FY economic growth forecast to 3.20%. In the same vein, the IMF reviewed Nigeria's 2024 economic growth projections downward to 3.00% citing the sustained Naira depreciation and suboptimal oil production.

The Debt Management Office (DMO) reported that Nigeria's public debt stock rose to NGN97.34trn (USD108.23bn) in 2023FY (from NGN87.91trn in 9M: 2023 and NGN46.25trn in 2022FY). This increase was primarily fueled by new domestic borrowings aimed at financing fiscal deficits combined with the impact of Naira depreciation on external borrowings. The DMO also disclosed that total domestic debt amounted to NGN59.12trn- c. 61% of the total debt stock, while external debt settled at NGN38.22trn- c.39%. Although the country's public debt is expected to remain high in the near term, ongoing debt management efforts and the anticipation of higher government revenue are expected to reduce reliance on debt.

Chart 3: Trend in Nigeria's Debt Profile (NGN'trn)



***Source:* NBS, Meristem Research**

Also, the NBS reported that total capital inflow increased by 2.62% YoY and 66.27% QoQ in Q4:2023 to USD1.09bn, marking the first quarterly increase in two years. This positive development is attributed to the rise in foreign portfolio investment (+8.59% YoY) and foreign direct investment (+118.42% YoY). The influx is credited to the elevated yield during the quarter and the bullish performance of the equity market, which attracted foreign investors. Across sectors, the production/manufacturing sector recorded the highest inflow with USD450.11mn, followed by the banking sector. Additionally, capital inflow into the oil and gas sector reached its year high after recording zero inflow in the second quarter of 2023.

Going forward, we anticipate that the currently elevated domestic fixed-income yields will stimulate investors' interest in Nigerian assets, particularly with an improvement in real rate of return. However, a downside to our expectation is the issue with illiquidity in the FX market which raises concerns on repatriation.

Similarly, the NBS reported a significant uptick in the country's trade, rising by 128.60% YoY and 42.50% QoQ to NGN26.80trn in Q4:2023, largely due to Naira's depreciation. Nonetheless, the nation experienced a trade deficit of NGN1.40trn for the first time in five quarters, driven by a 163.10% YoY surge in imports to NGN14.11trn, surpassing exports which increased by 99.56% YoY to NGN12.69trn. The oil sector dominated exports, while manufacturing accounted for approximately 63% of imports. Despite expectations of continued trade expansion, we anticipate the country's trade balance to remain in deficit due to projections of significant crude imports by the Dangote refinery and its impact on import values.

Macros

In Q1:2024, the Central Bank of Nigeria (CBN) implemented significant measures to stabilize the foreign exchange market. The Apex bank issued directives including the mandate that authorized dealer banks should expend Personal Travel Allowance (PTA) and Business Travel Allowance (BTA) payouts exclusively to electronic means, discontinuing cash transactions. Additionally, the CBN directed banks to limit the initial repatriation of export proceeds by International Oil Companies (IOCs) to 50%, with the remaining 50% to be gradually pooled over a 90-day period. Furthermore, the CBN eliminated the ±2.50% cap spread on interbank FX transactions and lifted restrictions on the sale of interbank proceeds, introducing the Naira as a payout option for international money transfers through CBN-approved International Money Transfer Operators (IMTOs). This provides recipients with the choice of receiving payments in just Naira.

Also, following its intervention of over USD300.00mn in the country's FX market, the CBN announced its decision to sell foreign exchange worth USD10,000 to eligible Bureau De Change (BDC) operators nationwide at the rate of NGN1,301.00/USD. This rate represents the lower band rate of executed spot transactions at NAFEM for the previous trading day. As per the directive, all BDCs are permitted to sell to end-users at a margin not exceeding 1.00% above the purchase rate from the CBN.

In furtherance to these moves, the CBN revealed that foreign investors acquired approximately USD1.00bn worth of Nigerian assets in February 2024. We attribute this increased inflow to elevated yield levels, which heightened investors' interest in the country's treasury instruments. The apex bank also announced the successful settlement of the remaining USD1.50bn, bringing the total amount settled to USD7.00bn. Subsequently, the country's external reserves surged to USD34.11bn in March 2024, the highest in eight months, attributed to increased foreign investment in government debt and higher diaspora remittances.

In our view, these measures align with the CBN's ongoing FX market reforms and its emphasis on a shift towards a market-driven price discovery system with improved transparency in foreign exchange dealings. Additionally, we opine that the successful implementation of the apex bank's broader policy measures could enhance liquidity in the foreign exchange market and contribute to stabilizing the Naira.

Key Expectations for Q2:2024

- ***Sustained increase in headline inflation.***
- ***For the stability in the currency to persist hinged on CBN reforms to curb speculative activities and improve liquidity as well as expectations of an improvements in foreign inflows.***
- ***Enhanced economic growth premised on improved oil output and better performance of the non-oil sector.***
- ***That the monetary authority will remain committed to its mandate on price stability, thus prompting direction of the MPC at its next meeting in May.***

Equities

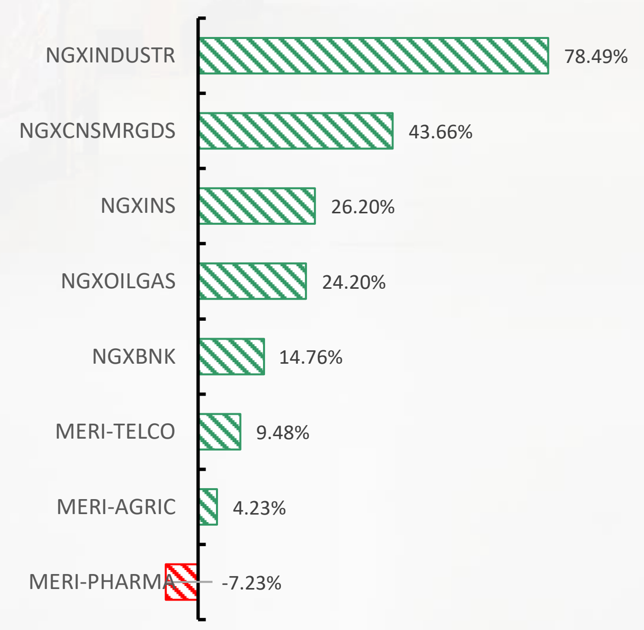
Local Bourse Remains Positive Despite Dampened Sentiment

Review

The Nigerian equities market maintained strong positive momentum in Q1:2024, primarily driven by buying interests on bellwether tickers in January (+35.28% MoM). However, in the succeeding months, performance was relatively mixed as sell-offs rocked the bourse - February (-1.16% MoM) and March (+4.58% MoM). The All-Share Index (**NGX-ASI**) returned **+39.84%** in Q1:2024, marking its highest quarterly gain since Q4:2020 to reach 104,562.10 points. Consequently, market capitalization increased to NGN59.12trn, compared to NGN40.92trn at the end of 2023. Reflecting heightened activity levels during the quarter, both volume and value traded rose by 36.24% and 60.69% to 34.86bn units and NGN683.24bn, respectively (vs 25.59bn units and NGN425.19bn in Q4:2023). Market breadth stood at 2.18x, with 85 stocks recording gains while 39 stocks ended the quarter in the red zone.

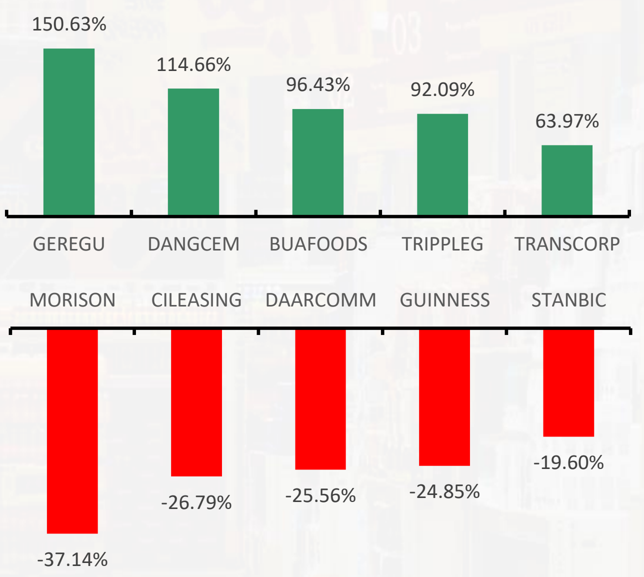
Furthermore, the bulls dominated across sectors as all sectoral indices under our tracking closed the quarter in the greens, save for **MERI-PHARMA** (-7.23% QoQ). The industrial goods index (+78.49% QoQ) had its highest quarterly gain on record due to heavy buying interests on **DANGCEM** (+114.66% QoQ) and **BUACEMENT** (+47.63% QoQ) in January**.**

Chart 4: Sectoral Returns in Q1:2024



***Source:* Bloomberg, Meristem Research**

Chart 5: Top Gainers and Losers for Q1:2024



Source: Bloomberg, Meristem Research

Investors Retain Varied Mood Amid MPC's 600bps Hike

The MPC implemented a 600bps cumulative increase in MPR during the quarter. The initial 400bps hike in February was unprecedented and caught investors off guard, leading to increased sell-off pressures amid the already dampened mood on the bourse. However, as highlighted in our Post-MPC report, the market largely anticipated the second 200bps hike in March, resulting in a muted response from investors who had already adjusted their positions accordingly.

Despite the elevated yields in the fixed income market which presents an attractive alternative for investors, there was no substantial rotation of funds out of the equities market. Moreover, Nigeria Exchange Group (NGX) reported a surge in foreign investors' participation in February 2024, reaching its highest in 3 months at 18.39% (vs 8.15% in Jan 2024 and 2023 avg. of 11.48%). We believe that the MPC's hawkish stance, along with ongoing reforms in monetary policy, has provided positive signals and clarity to foreign investors. Especially as the exchange rate stabilizes and the Naira appreciates (+18.24% in March) on the official window which have further boosted investors' confidence about repatriation of funds.

Equities

2023FY Financial Performance Sways Market Direction

Many corporates released their 2023FY financial results during the quarter, and as anticipated, performance was worse than the 9M:2023 results. Macroeconomic variables such as the depreciating exchange rate and inflation exerted pressure on cost line items and finance costs. For many sectors, foreign exchange (FX) loss was the major drag on their performance, leading some companies to record negative earnings and wiped-out shareholders' funds. This situation prompted significant sell-offs in some tickers, including large caps like **MTNN** (-12.12% QoQ) and **NESTLE** (-18.17% QoQ). On the other hand, the financial services sector registered FX revaluation gains.

Given that the Naira depreciated by 20.95% on the in Q1:2024, we expect a continuation of this weak performance in some selected sectors, with some sectors more exposed than others. In our report titled "*Impact of Currency Depreciation on Coverage Companies*," we conducted an analysis of the expected outcomes for Q1:2024 financials, outlining reasons for expected FX loss or gain as well as impact on profitability and shareholders' funds.

CBN Revises Banks' Capitalization Requirements

Towards the end of the quarter, the CBN released guidelines for the recapitalization of banks in the country. The apex bank increased the minimum capital requirement across banks and provided a 24-month window (effective from April 1, 2024 to March 31, 2026) for banks to raise the required amount of Tier 1 capital as per the new directives. The capital is restricted to share capital and share premium only, excluding retained earnings. The cumulative estimated funding gap for all listed banks amounts to NGN2.83trn.

This move is expected to strengthen banks' core equity base, thereby enhancing their capacity in the event of losses and drive further expansion in the banking sector. In response to the CBN's policy, we anticipate a surge in capital market activities.

Currently, FBNH, FIDELITY, WEMABANK, and ACCESSCORP have indicated their intentions to raise capital through right issues and private placements. In the near term, we anticipate other banks to follow suit, with right issue appearing as the most likely option to be explored by many banks. Additionally, there is a possibility of bank consolidations, particularly among those unable to meet the stipulated regulatory requirements.

Table 1: Revised Minimum Capital Requirement for Banks

Type of Bank	Authorization	MCR (NGN'bn)
Commercial	International	500.00
	National	200.00
	Regional	50.00
Merchant	National	50.00
Non-Interest	National	20.00
	Regional	10.00

Source: CBN, Meristem Research

Other Notable Occurrences and Corporate Actions

Transcorp Power Plc **(TRANSPOWER),** a subsidiary of Transnational Corporation Plc **(TRANSCORP),** successfully listed on the NGX on March 4th, 2024. The company is a power generating company focused on producing reliable and high-quality power for Nigeria and the West African region. **TRANSPOWER** listed 7.50 bn units at a price of NGN240.00 per share, resulting in a market capitalization of NGN1.80 trn. Following the listing, there was substantial buying interest on the ticker, driving the price by 57.08% QoQ to NGN377.00. Consequently, the ticker's market cap surged to NGN2.83trn, making it the 8th most capitalized stock on the bourse. **Using a blend of discounted cash flow models, we arrived at a fair value of NGN305.33 for the ticker, which represents an upside potential of 23.47% from its current price of NGN377.**

Access Holdings Plc (**ACCESSCORP**) announced that its subsidiary, Access Bank Plc, has entered into a binding agreement with Kenyan-based KCB Group Plc ("KCB") for the acquisition of the entire issued share capital of National Bank of Kenya Limited from KCB. National Bank of Kenya Limited is a historically strong and well-known bank in Kenya with a balance sheet of approximately USD1.10bn. This acquisition is subject to regulatory approvals from the Central Bank of Nigeria and the Central Bank of Kenya. **We believe that this transaction is in line with ACCESSCORP's African expansion strategy and will reposition it as a stronger and more significant player in the Kenyan market, which is the largest economy in East Africa. Additionally, this move is expected to bring confidence to shareholders amid changes in the bank's leadership, demonstrating a clear direction and commitment to diversification.**

Equities

Arbico Plc (**ARBICO**) has announced its intention to voluntarily delist from the Nigerian Exchange (NGX) after 46 years of being listed. Subject to approvals from regulatory authorities, the shares will be acquired by the company's majority shareholder (R28 Limited). **ARBICO** is a full-service building and civil engineering construction company in Nigeria with 148.50mn units of shares outstanding. **As the company has not yet disclosed the exit consideration for the delisting process, we advise shareholders holding the ticker to exercise caution. Other investors looking to buy the stock should seek clarity on the buy-out price and delisting procedure before taking position.**

As companies release their audited financial results for the 2023FY, 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 (%)
ACCESSCORP	24.50	27.70	12.64%	7.35%
FIDELITYBK	10.00	11.46	14.57%	8.00%
UCAP	23.20	28.39	22.38%	7.76%
WAPCO	38.05	58.43	53.56%	5.55%

**Prices are updated as of March 28th, 2024*

Summary of Key Expectations for Q2:2024

In Q2:2024, we anticipate a continuation of mixed sentiment in the Nigerian equities market, albeit leaning towards the positive. Market direction during the quarter is expected to be influenced by corporate actions and the release of Q1:2024 financial results. Specifically, we expect increased investor interest in banking stocks in anticipation of capital raises following the CBN's revision of minimum required capital. However, the expectation of weak performance from certain sectors may prolong the subdued mood in the market and could potentially trigger a fresh wave of selloffs if results are worse than expected.

Overall, we expect investors to maintain a cautious approach in the equities market, focusing on fundamentally strong stocks and capitalizing on profits when they have accrued substantially.

SSA Fixed Income

Sovereign Instruments Soar on Sustained Optimism

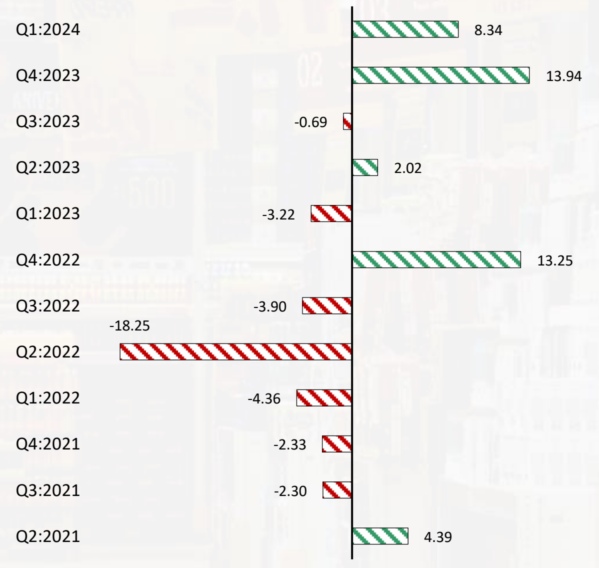
Our 2024FY outlook for African debt instruments remained bullish on hard-currency (FCY) offerings, while recommending investors to underweight local-currency (LCY) options. In line with our projection, the S&P African Hard Currency (FCY) instruments delivered a strong return of 7.75% (reaching 149.58 points) by the end of Q1:2024. This positive performance stemmed from renewed investor interest in Ghanaian, Egyptian, Zambian, and Nigerian markets, fueled by recent developments such as currency reforms and agreements with the International Monetary Fund (IMF). Conversely, LCY instruments experienced a peak return of 1.13% (reaching 1106.33 points) in February, followed by a decline to 1094.96 points by the close of Q1:2024. **While LCY options currently offer lower returns, we anticipate increased investors interest in them as macroeconomic conditions improve in specific African regions.**

In light of the attraction to the African markets, Nigeria's Eurobonds market was in generally bullish in Q1:2024, however with occasional sell pressures across the curve during the quarter. Particularly, the efforts by the monetary authority to implement policies aimed at addressing challenges in the country's FX market, spurred investors sentiment during the period. Furthermore, the hawkish stance of the monetary authority, evinced by the cumulative 600bps policy rate hike during the period, improve foreign investors activity in the Nigerian market. In the same vein, the issuance of Eurobond instruments by two SSA countries during the period which was significantly oversubscribed, underscored the attractiveness of SSA instruments during the period.

Expectation for Q2:2024

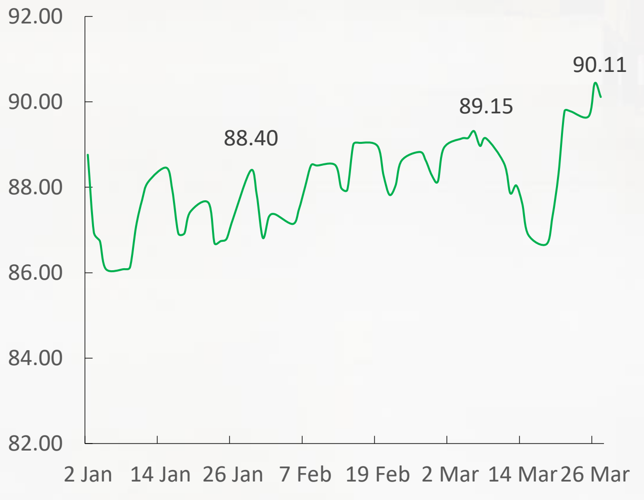
We expect a blend of factors to impact the Nigerian Eurobonds market in Q2:2024. On one hand, we anticipate a sustained positive sentiment, hinged on continued efforts by the monetary authority to stabilize the FX market. Also, expectations of potential rate cuts in advance markets during the period may further spur investors interest in the Nigerian instruments

Chart 6: S&P Hard Currency QoQ Return (%)



***Source:* S&P Global, Meristem Research**

Chart 7: Average Price (USD) Movement on Nigerian Movement in Q1:2024



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

Domestic Fixed Income

Lofty Heights for Treasury Yields

Review

Q1:2024 was an interesting period for the Nigerian domestic debt market as it was mostly characterized by rising yields, reflecting the monetary authority's objectives of liquidity and inflation targeting. The Primary Market Auctions (PMAs) for Treasury Bills conducted during the period underscore a clear increase in both government borrowing and investor interest compared to the previous quarter. The total allocation across PMAs reached NGN5.55trn, a significant jump from NGN2.65trn in Q4:2023. Similarly, investor demand surged, with subscriptions reaching NGN12.22trn (vs NGN7.44bn in Q4:2023). Notably, March witnessed the highest figures for both allocation and subscription throughout the quarter, highlighting a consistent upward trend in borrowing and investor activity.

The Monetary Policy Committee (MPC) held its inaugural meeting for the new administration in February, followed by another session in March, during which it implemented a cumulative 600bps hike in the MPR, raising it to 22.75%. This policy move reignited interest in the fixed income market, as evidenced in the average stop rates at the auction conducted post-March MPC meeting. Specifically, rates climbed to 16.24%, 17.00%, and 21.12% for the 91-day, 182-day, and 364-day instruments, respectively, marking a significant increase from the levels observed in Q4:2023 (7.00%, 10.00%, and 12.24%, respectively). This surge in rates came as no surprise, considering the steep decline in system liquidity recorded prior to the auction date of March 27, which plunged to a negative value of NGN16.28bn. Consequently, the auction experienced subdued investor demand, with the bid-to-cover ratio falling to 2.20x from 3.27x in Q4:2023.

Additionally, the CBN held an OMO auction, totaling NGN500.00bn across three offerings (95-day: NGN75.00bn, 179-day: NGN75.00bn, and 361-day: NGN350.00bn). Demand was strong (bid-to -offer: 2.3x), and resultantly, the CBN allotted NGN1.10trn across all tenors.

The Nigerian bond market mirrored the bearish trend of the Treasury Bill market. This quarter saw the issuance of three new bonds: FEB-2031, FEB-2034, and MAR-2027. The February offerings were particularly noteworthy, attracting significant investor participation. Despite a hefty NGN2.50trn offer, subscriptions came close, falling only c.24% short, reinforcing strong market appetite for government fixed income instruments. Resultantly, average bond yields climbed to a 20.13% by the end of Q1:2024, compared to 16.29% in Q4:2023.

In the secondary market, a predominantly bearish sentiment prevailed as investors offloaded some of their positions due to relatively tight system liquidity. Consequently, the average yields for T-bills and bonds rose to 17.66% and 19.41% respectively by the end of March, compared to 6.29% and 14.13% respectively at the end of Q4:2023.

Expectations for Q2:2024

With the Monetary Policy Rate (MPR) raised by 600bps, we anticipate a consequent upward adjustment in fixed income yields in the short term. Investors are expected to seek higher rates on risk-free instruments to align with the prevailing yield environment. While we anticipate a continued rise in yield levels on fixed income instruments, it's essential to note that the rate increment is not indefinite. We foresee periodic fluctuations in yield movements, influenced by factors such as system liquidity levels, investors' demand, and the necessity to moderate government borrowing costs.

Table 3: T-Bills Primary Market Auction Activity in Q1:2024

Ticker	Total Offer	Total Subscription	Allocation	Average Stop Rate
Jan	288.38	2,226.72	288.38	6.46%
Feb	1,265.50	4,220.88	2,589.35	17.96%
Mar	660.72	5,776.76	2,668.89	18.38%
Total	**2,214.60**	**12,224.36**	**5,546.62**	**14.27%***

Source: CBN, Meristem Research

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