MERISTEM

Macros and Market Insight

September 2024

Macros

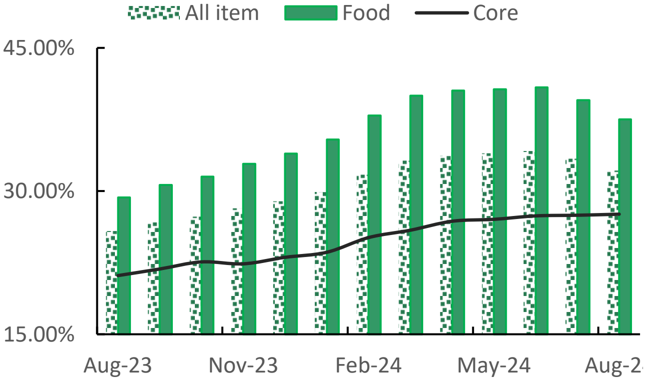
September's Economic Report Card: Progress amidst Lingering Challenges

Review

In September, Nigeria's macroeconomic landscape was influenced by several key developments. Notable events include the moderation in August's inflation figures, a rise in the country's trade surplus, and increased oil production volumes. Additionally, the Monetary Policy Committee (MPC) maintained its hawkish stance in its fifth meeting of the year.

The National Bureau of Statistics (NBS) reported that Nigeria's inflation rate eased for the second consecutive month by 125bps to 32.15% YoY in August 2024, from 33.40% in July 2024. This decline was largely attributed to a reduction in food inflation, which fell to 37.52% YoY (from 39.53% in July). Improved food supply during the ongoing harvest season led to lower prices for staples such as yams, tomatoes, and maize. However, core inflation rose by 11bps to 27.58% YoY (vs 27.47% in July), tied to increased transport costs due to fuel scarcity and higher fuel prices during the period. Additionally, both headline and food inflation continued to decline on a monthly basis, easing to 2.22% MoM and 2.37% MoM, respectively, in August (vs. 2.28% and 2.47% in July). However, core inflation remained on an upward trend, rising to 2.27% MoM from 2.16% in July.

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



Source: NBS, Meristem Research

We expect a further moderation in food inflation, supported by improved food supply, with additional crops like maize and soybeans becoming available as the current harvest season progresses and other government measures like the sale of subsidized rice.

Nonetheless, core inflation is anticipated to stay elevated in the near term, driven by rising fuel prices and volatility in the country's foreign exchange market.

At its September 2024 meeting, the MPC implemented another 50bps increase in the Monetary Policy Rate (MPR), marking the fifth consecutive hike this year and bringing the total increase to 850bps, with the MPR now at 27.25%. Furthermore, the committee increased the Cash Reserve Ratio (CRR) to 50.00% (+500bps) for Deposit Money Banks and to 16.00% (+200bps) for Merchant Banks while keeping all other parameters unchanged.

We believe this decision was largely influenced by several factors, including persistently high core inflation (despite a slowdown in headline inflation and food inflation), excess liquidity in the financial system and the need to sustain foreign investments to curb exchange rate volatility.

While these measures may help control liquidity and support foreign capital inflows, potentially stabilizing the exchange rate, they are likely to increase borrowing costs, putting additional strain on the real sector and dampening economic growth in the short term.

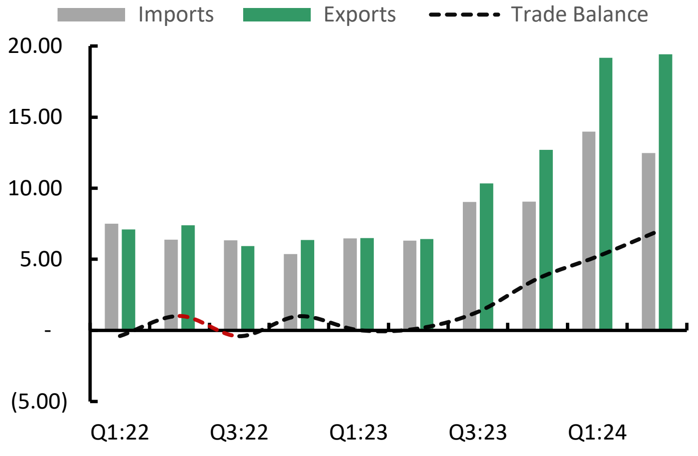
Additionally, the NBS reported that Nigeria's total trade surged by 150.39% YoY to NGN31.89trn in Q2:2024, up from NGN12.74trn in Q2:2023 (though it saw a 3.76% QoQ decline). This growth stemmed from increases in both exports and imports. Exports soared by 201.76% YoY to NGN19.42trn (+1.31% QoQ), while imports rose by 97.93% YoY to NGN12.47trn (10.71% QoQ). This led to a surplus of NGN6.95trn, +5114.99% YoY (from NGN133.18bn in Q2:2023). The rise in exports is largely attributed to the ongoing depreciation of the Naira and enhancements in crude oil production compared to the previous period. Meanwhile, the growth in imports can be primarily linked to the naira's depreciation, which increased the value of imported goods.

Notably, crude oil remained the primary contributor to exports, accounting for 74.98% of the total (down from 77.79% in Q2:2023), while manufactured goods constituted the largest share of imports at 44.71% (compared to 47.92% in Q2:2023).

Looking ahead, we anticipate the trade surplus to persist, supported by improved oil production that could enhance export figures and a more tempered rise in imports, likely influenced by a reduction in petroleum imports due to increased domestic refining activities.

Macros

Chart 2: Import, Export, Total Trade (NGN'trn)



Source: NBS, Meristem Research

The Nigerian Upstream Petroleum Regulatory Commission (NUPRC) reported a slight increase in crude oil production, reaching 1.35 million barrels per day (mbpd) in August, compared to 1.31mbpd in July. This growth was primarily driven by increased output from key terminals such as Bonny (4.89mbpd vs 4.58mbpd), Brass (0.72mbpd vs 0.66mbpd), and Forcados (8.13mbpd vs 6.81mbpd). However, the Qua Iboe (3.07mbpd vs 3.34mbpd) and Escravos (4.21mbpd vs 4.39mbpd) terminals experienced a decline.

Looking ahead, we expect continued improvement in oil production, underpinned by several positive developments in the oil and gas sector, including the Frontier Basin Exploration Fund, which aims to boost exploration activities in underexplored regions. Also, the recent auctioning of new oil blocks to attract investment and stimulate exploration, as well as the government's initiatives to curb oil theft and pipeline vandalism, are likely to enhance Nigeria's oil production capacity in the near term.

The Central Bank of Nigeria (CBN) has released its Monetary, Credit, Foreign Trade, and Exchange Policy Guidelines for Fiscal Years 2024-2025, reintroducing a 0.005% cybercrime levy on all electronic transactions. The reinstated levy aims to bolster the country's cybersecurity infrastructure, especially within the financial sector, while also serving as a supplementary revenue stream for the government. In addition, the CBN has implemented new restrictions on Bureau de Change (BDC) operations, capping single foreign exchange cash sales at USD5,000.00 per approved transaction. We expect this to increase transparency in currency transactions, ease pressure on FX demand, and promote greater stability in the FX market.

The Federal Executive Council has approved the Economic Stabilization Bills, incorporating recommendations from the Presidential Fiscal Policy and Tax Reforms Committee. The bill aims to amend tax and fiscal laws with key goals such as boosting investment in the gas sector, strengthening the Naira, promoting fiscal discipline, and creating jobs. Proposed changes include zero-rated VAT for exports, amendments to income tax laws to facilitate employment, tax relief for private sector players, the suspension of certain taxes on small businesses and vulnerable groups, and a tax identification consolidation initiative to broaden the tax base, provision of additional funding for the Students Loan Scheme, and facilitate investment in the country's oil and gas sector.

We believe that the successful execution of these policies could enhance the business environment, create more job opportunities, increase the competitiveness of the country's exports, improve government revenue in the medium to long term, and to quell demand pressures and support stability in the foreign exchange market.

Nigeria's unemployment rate climbed to 5.30% in Q1:2024, up from 4.10% in the same period in 2023, according to the NBS. This increase reflects the impact of ongoing macroeconomic challenges, which have hampered business growth and constrained job creation. Additionally, the employment-to-working-population ratio declined further to 73.20%, down from 76.60% in Q1:2023, highlighting the increasingly difficult business climate.

Looking ahead, the challenging economic environment is expected to keep employment levels subdued in the near term as businesses continue to grapple with insufficient growth to match the country's expanding labour force. However, with targeted government interventions—such as tax incentives for employers and policies aimed at boosting domestic manufacturing—there is potential for improvement in employment prospects over the medium to long term. These measures could stimulate business activity and help address the growing jobs deficit.

Summary of Key Expectations for October 2024;

- ***A slight uptick in the inflation rate, largely driven by an uptrend in core inflation.***
- ***Improved oil production hinged on positive reforms in the oil and gas sector.***
- ***Sustained trade surplus hinged on the expected improvement in oil production and the Naira's depreciation.***

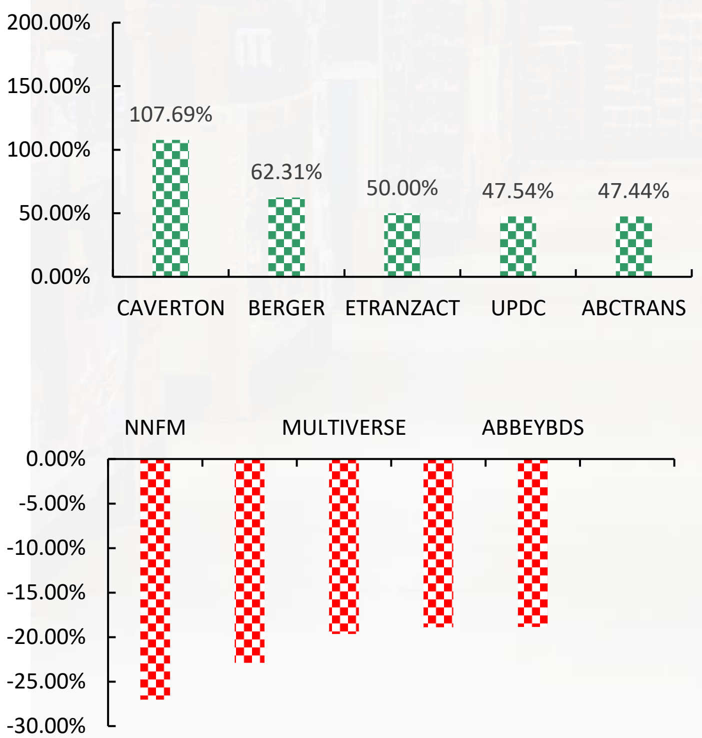
Equities

Rebounding Momentum; Bulls Hold Sway

Review

Activities in the equities market reflected a predominantly upbeat mood in September. The local bourse bucked the trend of negative monthly returns in previous months, as the NGX-ASI recorded a gain of 2.10% MoM to reach 98,987.42pts. Consequently, the Ytd Performance improved to 32.38% (vs. 29.01% in August). From our analysis, we observed major shareholders' buy-in on some bellwether tickers, which chiefly drove market direction northward during the month. For context, gains on **FBNH** (+34.09% Mtd), **UBA** (+17.58% Mtd) and **SEPLAT** (+10.00% Mtd) tilted the market to the green zone.

Chart 3: Top Gainers and Losers for September 2024



Source: NGX, Meristem Research

Chart 4: MoM Sectoral Returns in September 2024

NGX Indices	MtD
NGXBNK	+9.35%
NGXCNSMRGDS	+0.17%
NGXOILGAS	+6.61%
NGXINS	-0.14%
NGXINDUSTR	-0.20%
NGX-ASI	+2.01%
MERI-TELCO	+31.36%
MERI-AGRIC	+23.39%

Source: Bloomberg, Meristem Research

Other Notable Occurrences and Corporate Actions

During the month, Nigerian Breweries Plc (**NB**) received approval from the Securities and Exchange Commission (SEC) to commence a Rights Issue of 22.61bn ordinary shares of 50 kobo each, priced at NGN26.50 per share. The offer is structured to provide existing shareholders with eleven new shares for every five held as of July 12, 2024. NB has faced considerable challenges, including rising cost pressures, mounting debt, and increased foreign exchange (FX) losses. However, this Rights Issue is expected to provide much-needed relief by enabling the company to settle its FX-denominated debt, enhance its capital structure, and improve overall operational efficiency.

Additionally, Aradel Holdings Company (**SDARADEL**) has announced plans to redenominate its ordinary shares, reducing the nominal value from NGN10.00 to NGN0.50 per share. As a result, shareholders will receive 20 ordinary shares of NGN0.50 for every 1 share previously held at NGN10.00. This change could make the stock more affordable, potentially attracting new investors.

Equities

In another key development, Zenith Bank Plc (**ZENTIHBANK**) extended its right issue and public offer to September 23, 2024. The extension was aimed at bolstering its capital base in compliance with revised Central Bank of Nigeria (CBN) recaptitalisation requirements. The rights issue allows existing shareholders to purchase additional shares at NGN36.00, while the public offer was opened to new investors at NGN36.50 per share. **We expect that this extension will further bolster its operations, enhance market presence, and improve the company's balance sheet.**

Lastly, Fidson Healthcare Plc (**FIDSON**) announced a partnership agreement with three Chinese firms- Jiangsu Aidea Pharma, Nanjing PharmaBlock, and the China-Africa Development Fund. The partnership aims to establish a joint venture pharmaceutical plant in Nigeria, focusing on improving healthcare delivery, particularly in HIV treatment. **We anticipate this collaboration to significantly increase FIDSON's production capacity and may spur further collaborations in other geographic locations.**

Summary of Key Expectations for October 2024

We anticipate market sentiment to be largely mixed in October, hinged on a blend of factors. On the one hand, we foresee the continued strong performance of banking stocks, alongside potential recoveries in other sectors, which is likely to drive gains in coming weeks. Furthermore, likely 9M:2024 earnings releases may also bolster the favourable sentiment. However, we note that the gradual upticks in treasury yields due to the recent 50 bps hike could occasionally sway investors' sentiments toward fixed-income assets. Overall, our outlook is subtly tilted to a bearish bias for October.

Fixed Income

From Bearish Beginnings to Bullish Trends

Review

In September, the fixed income primary market opened on a bullish note as nominal yield averaged 18.91% compared to 20.17% at the close of the last auction in August. A total of four primary market auctions were executed this month including three Treasury Bills (T-bills) as is the case at the end of every quarter and one domestic bond. Additionally, the monetary authorities conducted three Open Market Operations (OMO) auctions. There was an interesting interplay of yields and liquidity during the month as yields inched higher following the MPC's decision to hike the monetary policy rate and increase the cash reserve ratio for commercial and merchant banks.

At the T-Bills Primary Market Auction (PMA) in September, the CBN offered a total of NGN622.74bn, slightly lower than the NGN626.07bn offered in August. Demand surged slightly higher with total subscription at NGN1.99trn compared to NGN1.51trn reached in August, reflecting high system liquidity. As a result, the subscription-to-offer ratio jumped to 3.21x from 2.42x in August, indicating sustained demand. The total amount allotted also increased to NGN622.73bn, compared to NGN507.13bn in the previous month. During the period, yields on the trio of instruments showed notable movements. Rates declined at the first two auctions, falling to 17.00%, 17.50%, and 18.94%, and further to 16.63%, 17.00%, and 18.59%, down from 18.20%, 19.20%, and 20.90% in the previous month. This was largely reflective of high liquidity and the government's ongoing efforts to reduce borrowing costs. However, following the MPC's decision to raise the MPR by 50bps, rates edged up in the final auction of the month by 37bps, 50bps, and 141bps, reaching 17.00%, 17.50%, and 20.00%, respectively after four consecutive auctions of lower yields.

In the bonds market, the Debt Management Office (DMO) offered a total of NGN150bn in September, a 21.05% reduction from the NGN190bn offered in August. This decline aligns with the government's lower borrowing needs, likely supported by alternative funding sources, particularly the proceeds from the domestic dollar-denominated bond issued last month. The auction featured the reopening of three bonds—APR 2029, FEB 2031, and MAY 2033. Total subscriptions reached NGN414.88bn, slightly down from NGN460.18bn in August, while NGN264.53bn was allotted, compared to NGN374.75bn in the previous month. Despite this, marginal rates dropped across all maturities, with APR 2029 falling by 130bps, FEB 2031 by 91bps, and MAY 2033 by 145bps, closing at 19.00%, 19.99%, and 20.05%, respectively. This decline in rates can be attributed to elevated system liquidity, bolstered by FAAC inflows (NGN1.20trn) and bond coupon payments.

In line with the CBN's liquidity management strategy, three Open Market Operation (OMO) auctions were held in response to significant inflows during the period. and coupon payments during the month. Throughout these auctions, investor preference skewed towards the longest-tenored instrument, with no recorded subscriptions or sales for shorter tenors. Overall, NGN1.25trn was sold, a significant decrease from NGN2.35trn in August. At the first OMO auction in September, the stop rate fell slightly to 21.80%, down from 21.87% in August. However, following the CBN's decision to raise the benchmark interest rate by 50bps to 27.25% and adjust the Cash Reserve Ratio for commercial and merchant banks to 50.00% and 16.00%, respectively, rates at the subsequent two auctions spiked to 24.36%. The higher rates align with the CBN's objectives of liquidity management and inflation control.

Meanwhile, the secondary market traded on a mixed note, with average T-bill yields increasing to 21.91% (up from 21.21% in August), and average bond yields falling to 18.75% (from 18.96% in August), reflecting a mix of system liquidity and investors repositioning to capitalize on higher yields.

Outlook:

We anticipate a moderate rise in yields, as system liquidity tightens in the short to medium term due to the Central Bank's hawkish approach to absorbing excess liquidity. While we acknowledge the reduced borrowing needs of the government, on the balance, we anticipate that yields will trend upwards to sustain investor interest in the fixed income market.

Eurobonds

Declining Yields Signal Renewed Investors Confidence

The Nigerian Eurobonds market experienced mixed performance during the month. Early on, market sentiment was bearish, with yields gradually rising to 9.81%. However, after the U.S. Federal Reserve implemented a 50bps rate cut, investors grew more optimistic about Nigerian Eurobonds, given their enhanced appeal compared to yields in advanced economies. This shift spurred a decline in yields, which dropped to 9.28% by the end of the month, reflecting heightened demand for the instruments.

The bullish momentum in the Nigerian Eurobond market signals a positive shift in sentiment, with Nigeria's yields becoming increasingly attractive. Investors also appeared more confident in Nigeria's fiscal management, supported by two consecutive months of declining inflation and the additional 50bps rate hike toward the month's end. Furthermore, the rate-cutting cycles in other emerging markets, such as South Africa and Ghana, following the U.S. decision, likely fueled investor confidence in Nigerian Eurobonds. This surge in demand was evident through price increases across all Eurobond instruments in September.

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