Nigeria: Economic Outlook
Top 10 themes for 2018

February 2018
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**Oil prices still lower for longer**

**Oil, Brent (USD/bbl)**

- A balanced oil market will keep the oil price at USD60/bbl, 10% higher than 2017.
- An extension of the oil production cut agreement through 2018 should provide a floor for prices at USD55/bbl.
- Rising US shale output remains a key supply risk which would cap oil prices around USD70/bbl.

*Source: IEA, OPEC, PwC Analysis*
Economic growth gets a boost from high oil prices

- Real GDP growth to reach 2.0% y/y on improvements in net exports and domestic demand.
- Exports are likely to outpace imports on strong oil export revenues and shrinking import demand.
- Investments will benefit from an improving investment climate. However, some of this growth will be offset by uncertainty usually associated with election cycles in Nigeria.

Sources: NBS, PwC Analysis
Inflation declines sharply, driven mainly by base effects

Average annual inflation rates (y/y)

- Headline inflation decelerates 4.3 ppt to an average of 12.2% y/y, driven by base effects from the relatively high inflation rates in H1’17
- Food inflation moderates to 14.0% y/y - the lowest since June 2016, mainly a reflection of improved food output in H2’18
- Core inflation slows to 11.2% y/y as the impact of base effects more than offsets inflationary pressures from stronger consumer demand and higher transport costs

Sources: NBS, PwC Analysis

Note: The inflation figures quoted refer to the average for the year
**Monetary Policy Rate set to fall, and then rise**

**Monetary Policy Rate (MPR)**

- 150bps increase in MPR 16 months prior to April 2011 elections
- 100bps increase in MPR 15 months prior to March 2015 elections

**Projections**

- 200bps reduction in MPR in March 2018
- 200bps increase in September 2018

**Sources:** CBN, PwC Analysis

- We expect only one rate cut in 2018 which would likely be capped at 200bps. The need to keep rate differentials attractive means OMO issuances would become more aggressive.
- To offset the impact of pre-election spending and currency volatility, we expect a 200bps increase in the MPR to 14% at the September meeting.
- Moderating inflation, exchange rate stability and a fragile economic recovery provide room for a rate cut.

**Nigeria: Economic Outlook**

- **Economic Growth**
- **Inflation Rate**
- **Oil price**
- **Fiscal Finances**
- **Exchange Rate**
- **Investment**
- **Petrol Supply: Scenarios**
- **2019 Elections**
- **Three Emerging Scenarios**
- **Nigeria’s Risk Matrix**
Government’s fiscal deficit expands above budget

Federal Government expenditure, revenue and fiscal deficit (% of GDP)

- We expect revenues to underperform budget by c.34% as a shortfall in non-oil revenues offsets the impact of the strong recovery in oil revenues
- Consequently, debt service to revenue expands to 45%, higher than the projected 31% in the budget
- Fiscal deficit widens by 67% to NGN3.4 trillion (2.4% of GDP). We expect that the deficit will be funded by an increased issuance in the domestic bond market

Source: Budget Office, PwC Analysis
Recent history suggests that election cycles are associated with increased foreign exchange demand

**External Reserves (USD’ billion)**

- A sharp 24% decline between January 2010 and May 2011
- A sharp 30% decline between January 2014 and May 2015

**Interbank Rate (NGN/USD)**

- A significant 23% depreciation between January 2014 and May 2015
- A mild 4% depreciation between January 2010 and May 2011

Source: CBN, PwC Analysis

Note: The extent of depreciation in the exchange rate depends on the broad macro-economic environment during the election season.
The exchange rate depreciates in the I&E window

Exchange rate (Official vs I&E Window vs Parallel market)

1. With the outlook on the oil price and level of reserves accretion (USD40.6 billion*), we expect that the CBN would maintain the exchange rate peg of NGN305/USD at the CBN window.

2. In H2’18, we estimate a 7% exchange rate depreciation in the I&E window to NGN386/USD, as FX demand increases and foreign investments slow ahead of the 2019 elections.

3. Overall, the CBN maintains its multiple exchange rate regime, sustaining its intervention in the various FX markets.

Source: CBN, PwC estimates

*External reserves data is as at January 30 2018
Stable investment climate supports increase in FPI and FDI

**Key Considerations**

1. FPI increases moderately, due to strong foreign investor interest. However, we expect a slowdown in FPI in H2’18, driven by uncertainty ahead of the elections.

2. FDI advances slightly, driven by a favourable investment climate and broad macroeconomic stability.

3. **Key risks to foreign investment include:**
   - Declining interest rate differentials as advanced economies continue to tighten policy rates.
   - Political instability ahead of the 2019 elections drives uncertainty around government policies.

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**Foreign Investment, 2014 - Q3’2017 (USD’million)**

- Foreign Portfolio Investment
- Foreign Direct Investment

Source: CBN, NBS, PwC estimates
PMS Deregulation scenarios: petrol prices will likely be maintained at NGN145/litre

How much could Nigerians pay for petrol?

<table>
<thead>
<tr>
<th>Exchange rate (NGN/USD)</th>
<th>Oil price (USD/bbl.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>50</td>
</tr>
<tr>
<td>285</td>
<td>144</td>
</tr>
<tr>
<td>325</td>
<td>160</td>
</tr>
<tr>
<td>365</td>
<td>176</td>
</tr>
<tr>
<td>405</td>
<td>192</td>
</tr>
</tbody>
</table>

- The grey area in the table are the possible retail prices of petrol per litre, given changes in exchange rate and oil price.
- Note: The estimates are based on PPPRA's previous petrol pricing template as at May 2016, margins are held constant.

Source: PPPRA, PwC estimates

Scenario A

- NNPC continues to be the sole importer of petrol. Intermittent scarcity in the supply of petrol persists.
- Impact on headline inflation is marginal. Estimate remains around 12.2% y/y in 2018, in line with our projection.

Scenario B

- The exchange rate assumption is marked to NAFEX; petrol prices increase by at least 57%.
- Marketers resume importation of petrol, with improved supply.
- Headline inflation accelerates to 15.0% y/y in 2018, 180bps above our baseline estimate.
New parties, defections and political truces; the pre-election season gets underway

What we know...

Presidential elections: 16 February 2019

*No of Parties: 68

Emerging three horse race?

All Progressives Congress

Peoples Democratic Party

A new coalition?

New alliances are being formed by prominent politicians and old guards to upset the dominance of the APC and PDP

Unwritten rule

The zoning principle

- Zoning implies the sharing or rotation of public office based on region, ethnicity or religion aimed at reducing domination or marginalization of a group(s) of people

What does historical data tell us?

- Reviewing election results from the past 2 presidential election cycles, we observed a shift in the voting pattern of voters in the South-West and the North-Central states in the 2015 elections

- The question is, which states will swing in 2019?

PwC Analysis

Which states will swing in 2019?

2011 Presidential Election

CPC
Muhammadu Buhari

PDP
Goodluck Jonathan

ACN
Nuhu Ribadu

2015 Presidential Election

APC
Muhammadu Buhari

PDP
Goodluck Jonathan

Note: CPC and ACN merged into APC in 2013

*As at January 2018
A stable political environment key to sustaining Nigeria’s economic recovery

**Real GDP Growth**

![Graph showing Real GDP Growth from 2017 to 2022 with three scenarios: Scenario 1, Scenario 2, and Scenario 3.](source: NBS, PwC estimates)

**Our Assumptions**

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Oil price (USD/bbl.)</th>
<th>Oil Production (mbpd)</th>
<th>Structural reforms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scenario 1: Accelerated Policy reforms</td>
<td>60</td>
<td>2.2</td>
<td>Fast-paced implementation of structural reforms, particularly those related to the business environment</td>
</tr>
<tr>
<td>Scenario 2: Weak policy implementation</td>
<td>60</td>
<td>2.2</td>
<td>Sluggish implementation of structural reforms, with the drive for import substitution progressing at a slow pace</td>
</tr>
<tr>
<td>Scenario 3: Heightened political risk</td>
<td>60</td>
<td>1.7</td>
<td>Political tension accelerates in the wake of 2019 general elections, negatively impacting policy implementation</td>
</tr>
</tbody>
</table>
## Lower oil prices, disruptions to crude oil production, and political instability are the major near term risks

<table>
<thead>
<tr>
<th>Risks</th>
<th>Description</th>
<th>Potential impact</th>
<th>Likelihood of occurrence</th>
<th>Time horizon</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lower oil prices</td>
<td>• Failure of OPEC members to comply with production cuts agreement and increasing shale production</td>
<td>★</td>
<td>★</td>
<td>Short to medium term</td>
</tr>
<tr>
<td>Slowdown in key economies</td>
<td>• Slowdown in economies with strong trade relations with Nigeria, particularly China, the UK, the US and India</td>
<td>★</td>
<td>★</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td>Monetary policy normalization</td>
<td>• Ongoing monetary policy normalization in the US could lead to a reversal of foreign capital and restrict further flows</td>
<td>★</td>
<td>★</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td>High inflation</td>
<td>• Pre-election and 2018 budget spending</td>
<td>★</td>
<td>★</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td>Oil production disruption</td>
<td>• Adjustments of petrol prices and power tariff</td>
<td>★</td>
<td>★</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td>Political risk/Heightened insecurity</td>
<td>• Pre-election uncertainties could elevate political tensions, and leadership succession could hamper policy continuity</td>
<td>★</td>
<td>★</td>
<td>Medium term</td>
</tr>
<tr>
<td></td>
<td>• Continuous insurgency in the Northern region</td>
<td>★</td>
<td>★</td>
<td>Short to Medium term</td>
</tr>
</tbody>
</table>
### Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>APC</td>
<td>All Progressives Congress</td>
</tr>
<tr>
<td>ACN</td>
<td>Action Congress of Nigeria</td>
</tr>
<tr>
<td>BBl</td>
<td>Barrel of Crude Oil</td>
</tr>
<tr>
<td>CBN</td>
<td>Central Bank of Nigeria</td>
</tr>
<tr>
<td>CPC</td>
<td>Congress for Progressive Change</td>
</tr>
<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
</tr>
<tr>
<td>FPI</td>
<td>Foreign Portfolio Investment</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>I&amp;E</td>
<td>Investors and Exporters Window</td>
</tr>
<tr>
<td>MPC</td>
<td>Monetary Policy Committee</td>
</tr>
<tr>
<td>MPR</td>
<td>Monetary Policy Rate</td>
</tr>
<tr>
<td>NAFEX</td>
<td>Nigerian Autonomous Foreign Exchange Rate Fixing</td>
</tr>
<tr>
<td>NBS</td>
<td>National Bureau of Statistics</td>
</tr>
<tr>
<td>NGN</td>
<td>Nigerian Naira</td>
</tr>
<tr>
<td>NNPC</td>
<td>Nigerian National Petroleum Corporation</td>
</tr>
<tr>
<td>OMO</td>
<td>Open Market Operation</td>
</tr>
<tr>
<td>PDP</td>
<td>People's Democratic Party</td>
</tr>
<tr>
<td>PPPRA</td>
<td>Petroleum Products Pricing Regulatory Agency</td>
</tr>
<tr>
<td>USD</td>
<td>United States Dollar</td>
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</table>
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Thank you

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