Nigeria: Economic Outlook
Top 10 themes for 2018

February 2018

pwc

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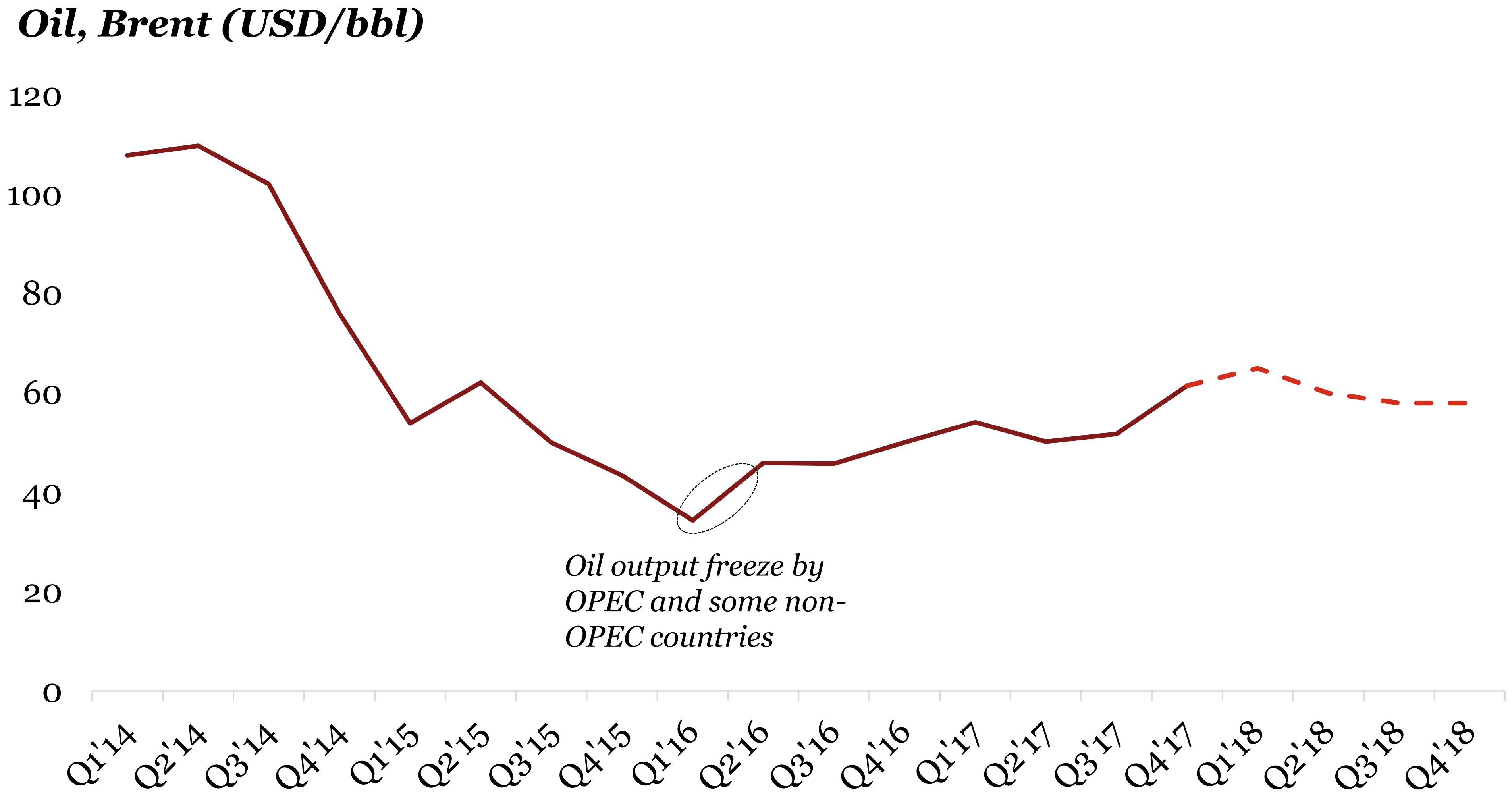
Contents

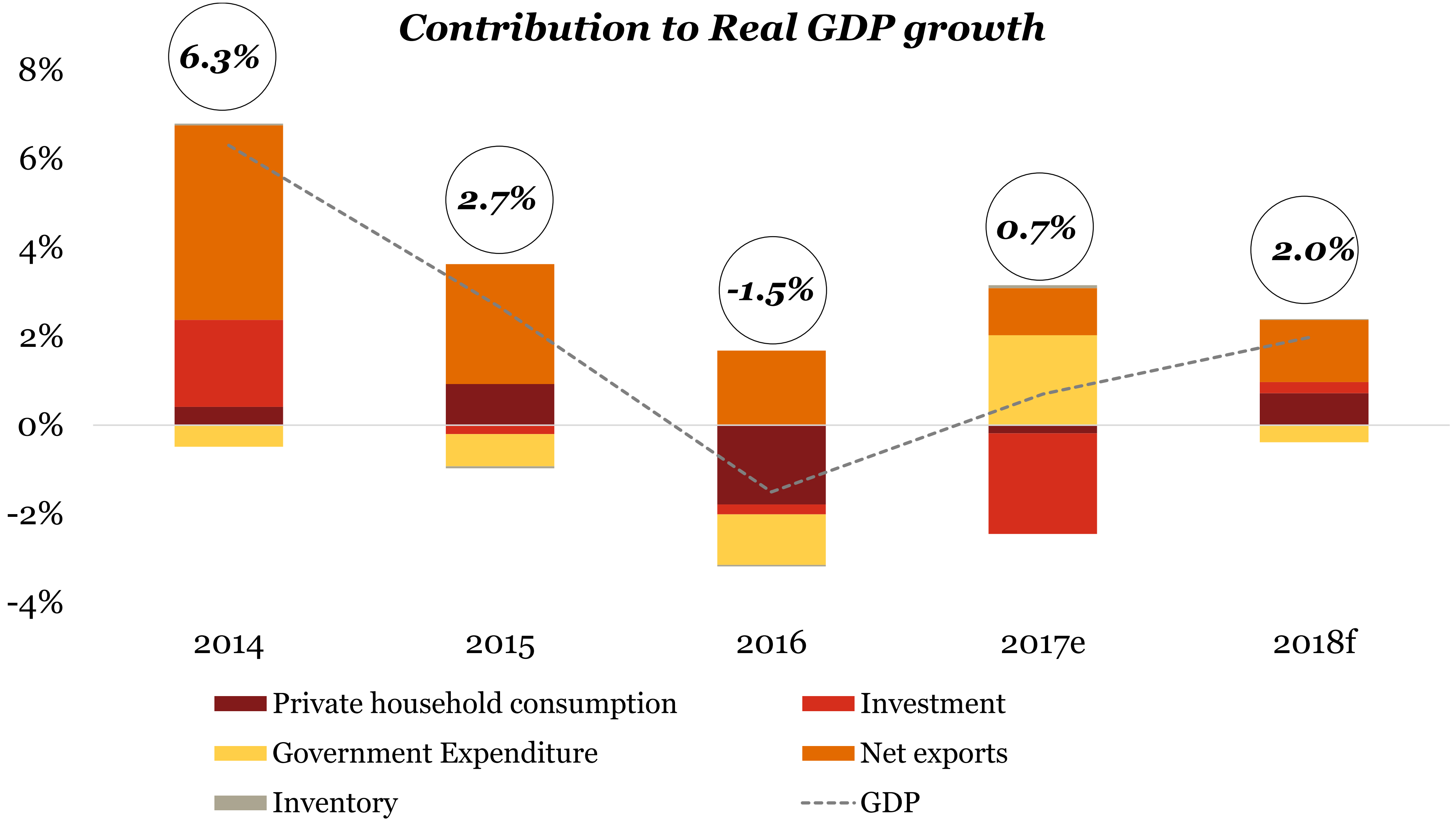
Oil prices still lower for longer



Source: IEA, OPEC, PwC Analysis

- 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

Economic growth gets a boost from high oil prices

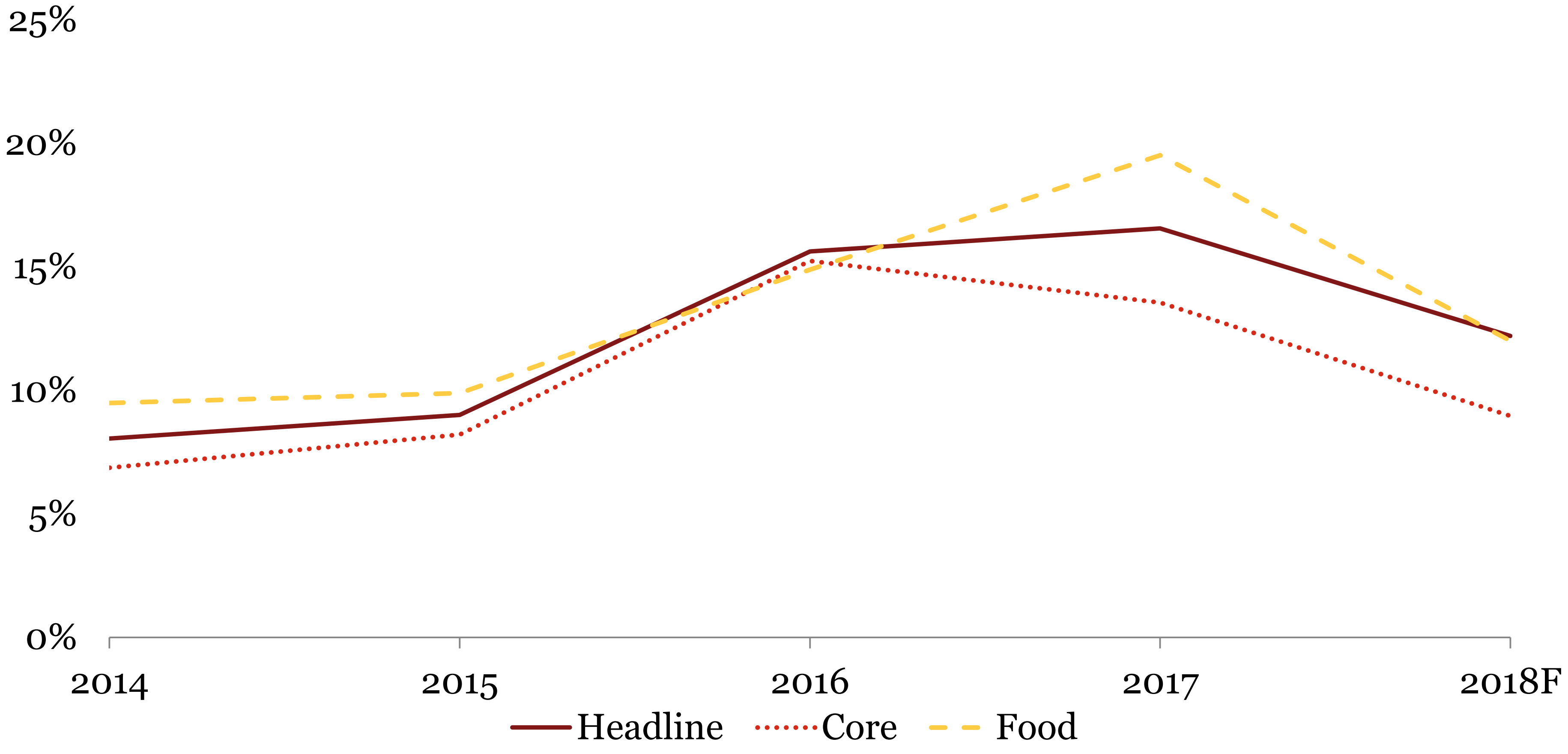


Sources: NBS, PwC Analysis

- 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

Inflation declines sharply, driven mainly by base effects

Average annual inflation rates (y/y)

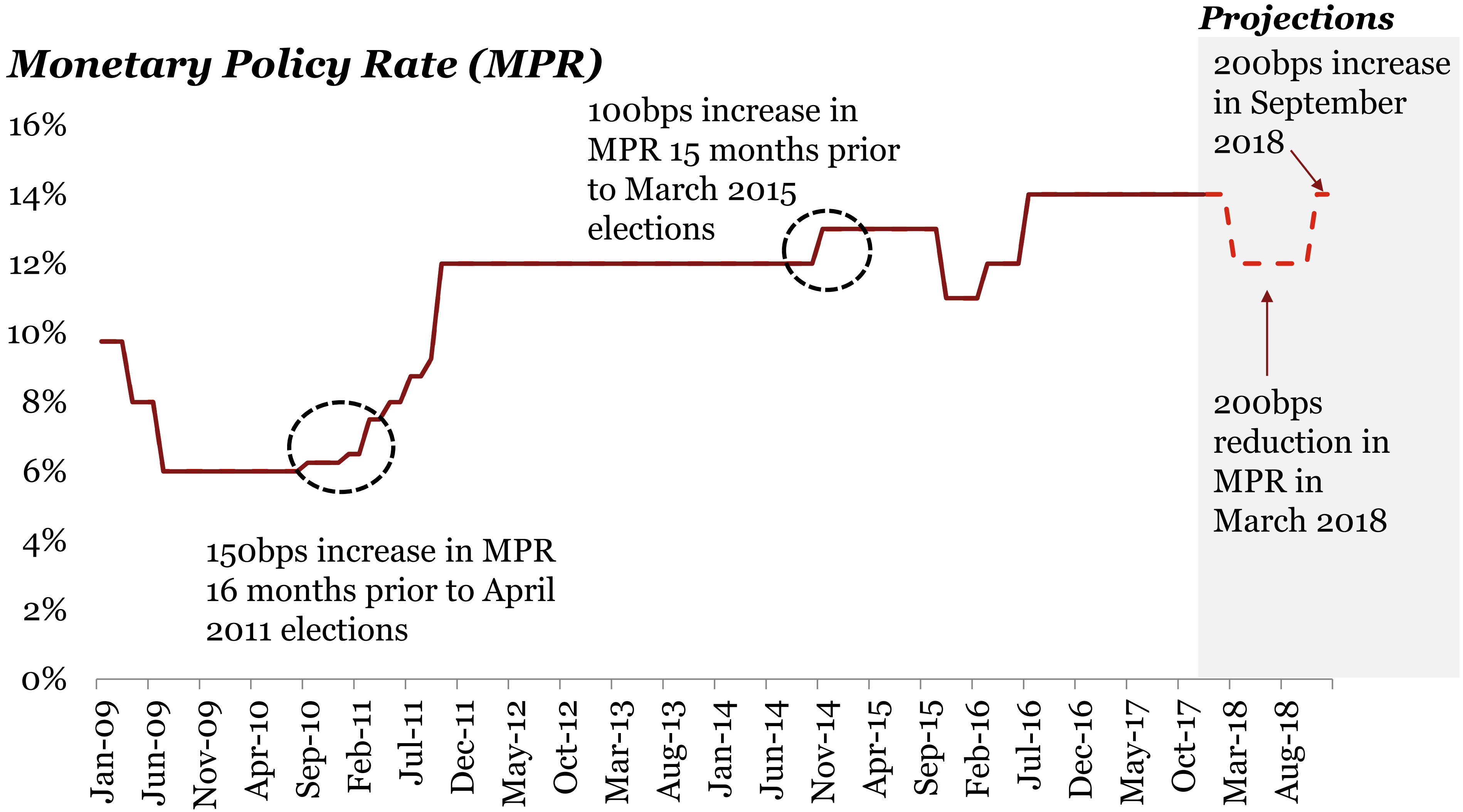


Sources: NBS, PwC Analysis

Note: The inflation figures quoted refer to the average for the year

- 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

Monetary Policy Rate set to fall, and then rise

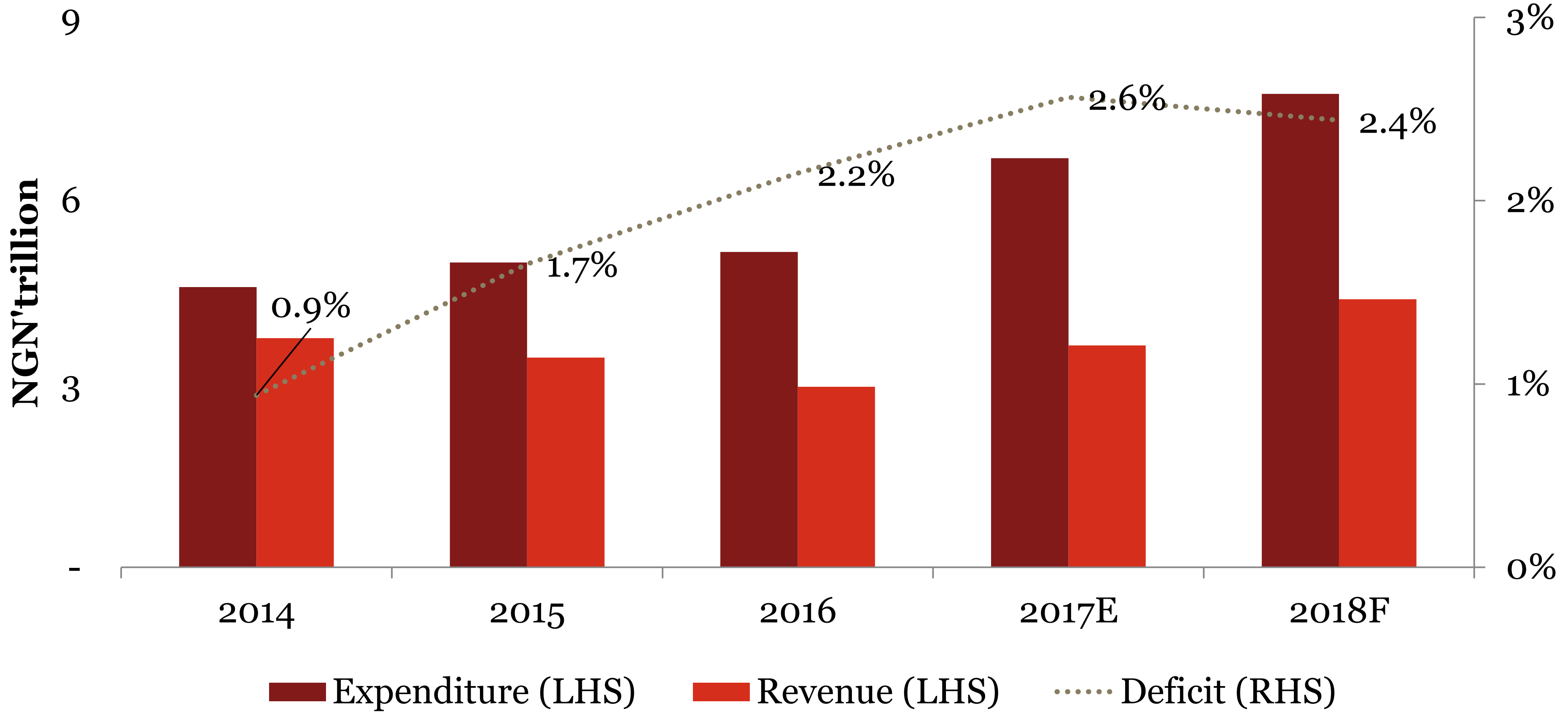


Sources: CBN, PwC Analysis

- Moderating inflation, exchange rate stability and a fragile economic recovery provide room for a rate cut
- 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

Government's fiscal deficit expands above budget

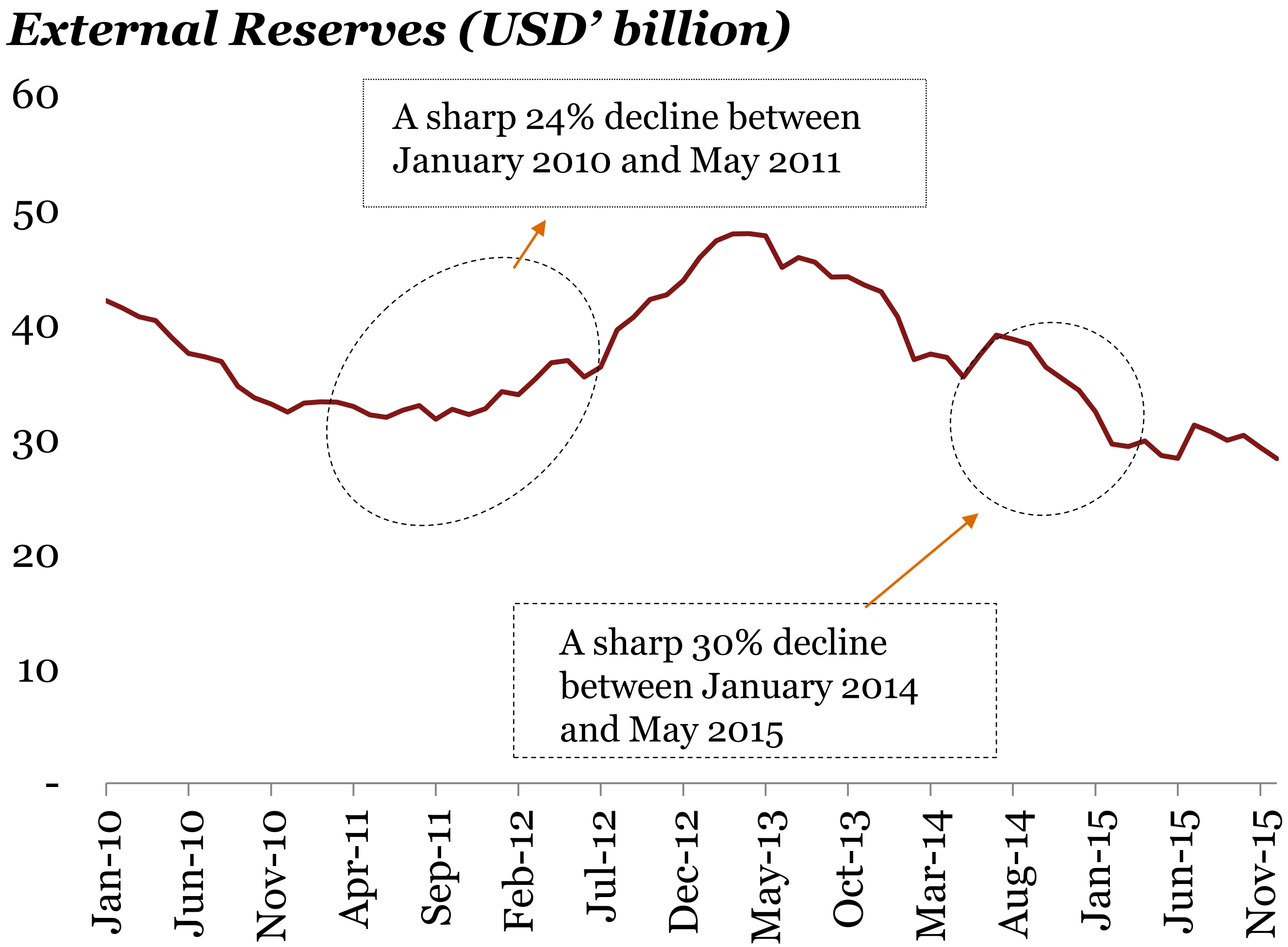
Federal Government expenditure, revenue and fiscal deficit (% of GDP)



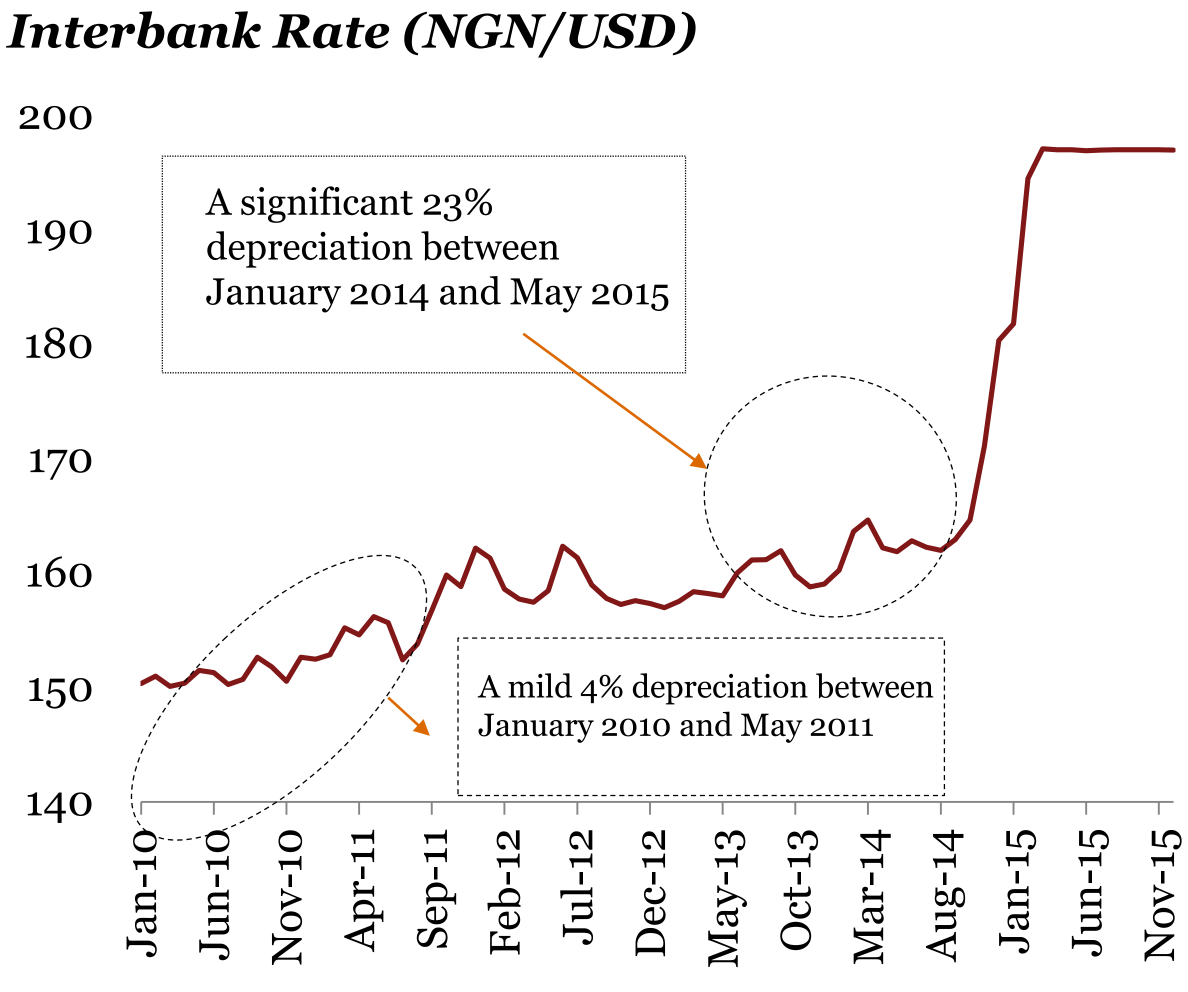
Source: Budget Office, PwC Analysis

- 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

Recent history suggests that election cycles are associated with increased foreign exchange demand



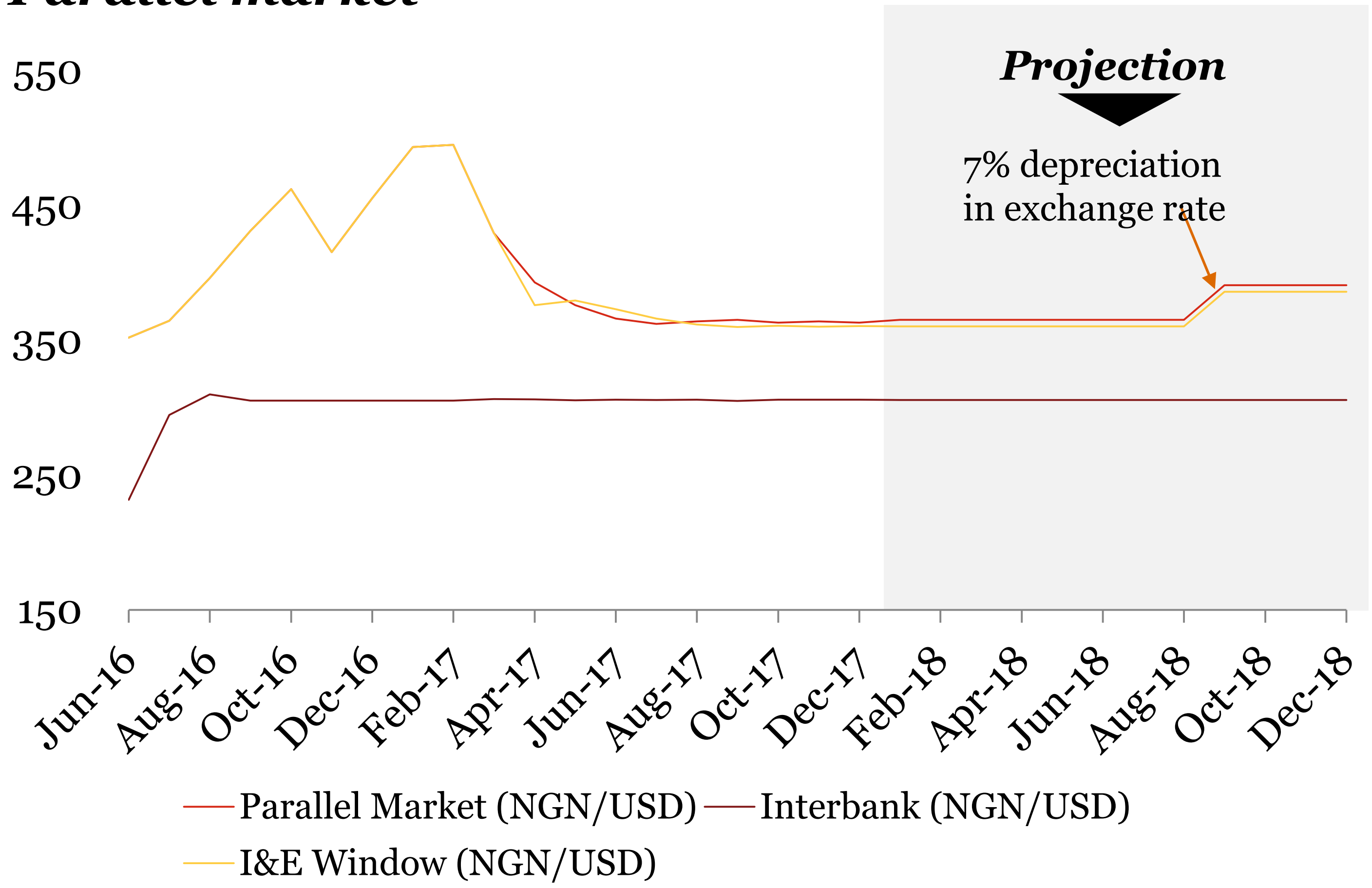
Source: CBN, PwC Analysis



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

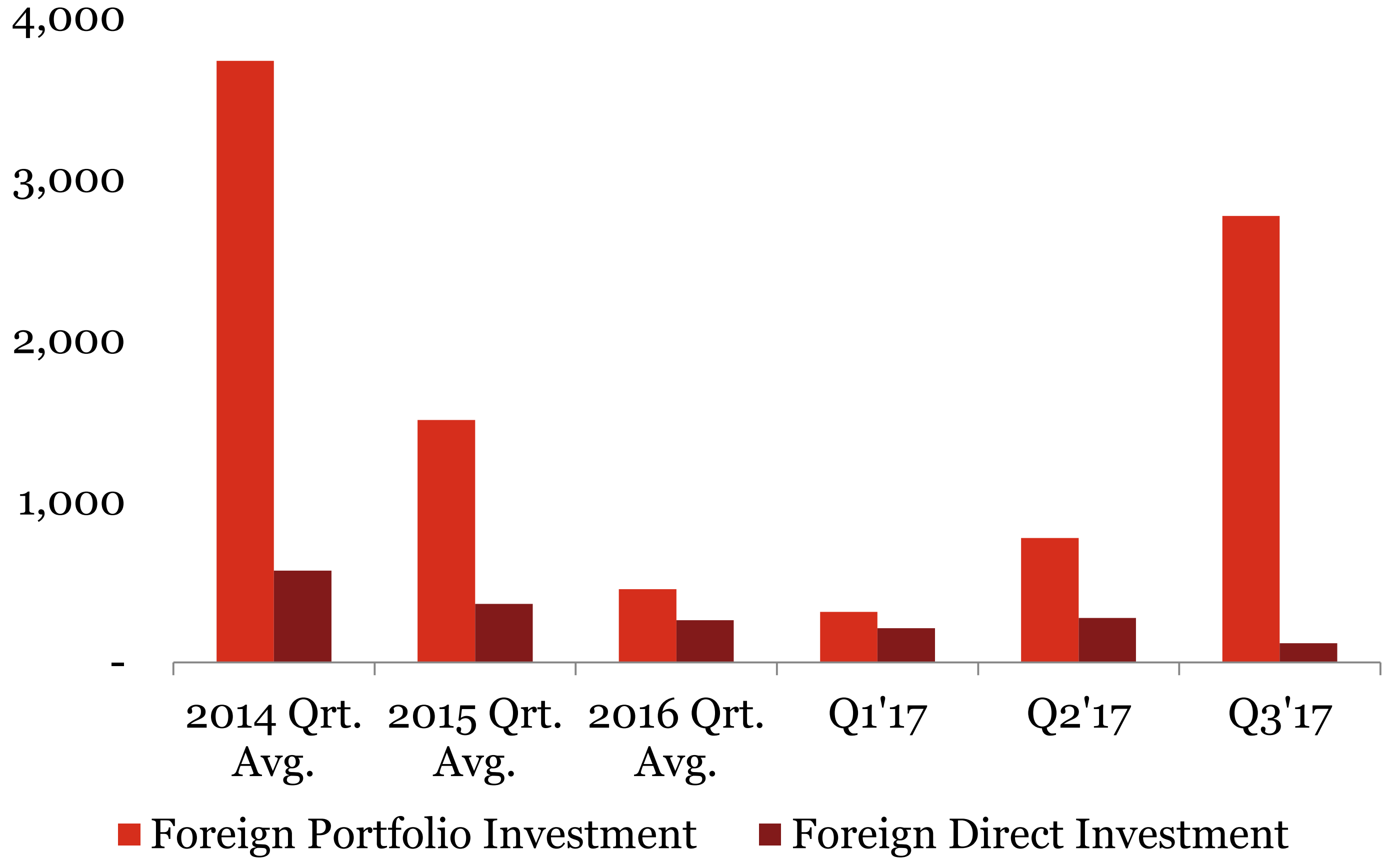
2 In H2'18, we estimate a 7% exchange rate depreciation in the I&E window to NGN386/USD, as FX demand increases and foreign investments slow ahead of the 2019 elections

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

Foreign Investment, 2014 - Q3'2017 (USD'million)



Source: CBN, NBS, PwC estimates

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

PMS Deregulation scenarios: petrol prices will likely be maintained at NGN145/litre

How much could Nigerians pay for petrol?

Exchange rate (NGN/USD)	Oil price (USD/bbl.)			
	50	60	70	80
285	144	164	184	205
325	160	183	206	229
365	176	202	228	254
405	192	221	250	278

- *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*

Current administered price (red)

Estimated retail price of PMS under a full deregulation scenario (green)

Source: PPPRA, PwC estimates

Scenario A

Fuel subsidy

- 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

Full Deregulation

- 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?

	Parties
All Progressives Congress	APC
Peoples Democratic Party	PDP
A new coalition?	?

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

** As at January 2018*

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?

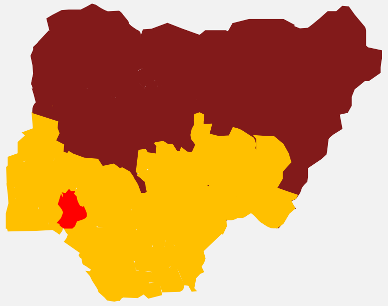
- Reviewing election results from the past 2 presidential election cycles, we observed a shift in the voting pattern of voters in the South-West and the North-Central states in the 2015 elections

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

PwC Analysis

Which states will swing in 2019?

2011 Presidential Election

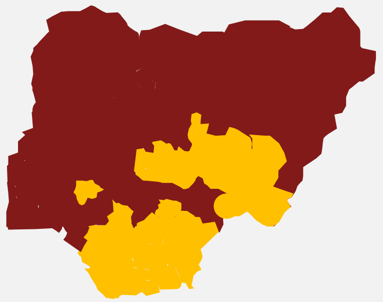


CPC Muhammadu Buhari

PDP Goodluck Jonathan

ACN Nuhu Ribadu

2015 Presidential Election



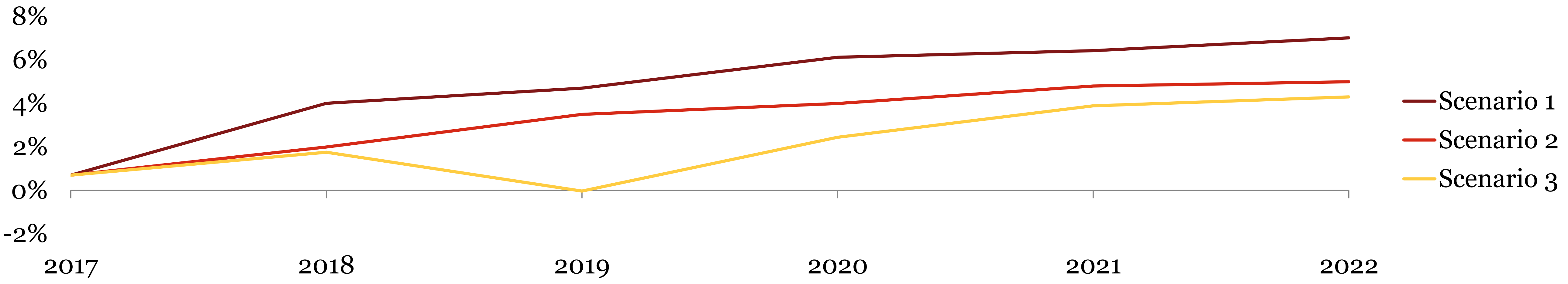
APC Muhammadu Buhari

PDP Goodluck Jonathan

Note: CPC and ACN merged into APC in 2013

A stable political environment key to sustaining Nigeria's economic recovery

Real GDP Growth



Source: NBS, PwC estimates

Our Assumptions	*Oil price (USD/bbl.)*	*Oil Production (mbpd)*	*Structural reforms*
Scenario 1: Accelerated Policy reforms	60	2.2	Fast-paced implementation of structural reforms, particularly those related to the business environment
Scenario 2: Weak policy implementation	60	2.2	Sluggish implementation of structural reforms, with the drive for import substitution progressing at a slow pace
Scenario 3: Heightened political risk	60	1.7	Political tension accelerates in the wake of 2019 general elections, negatively impacting policy implementation

Lower oil prices, disruptions to crude oil production, and political instability are the major near term risks

Risks	Description	Potential impact	Likelihood of occurrence	Time horizon
Lower oil prices	• Failure of OPEC members to comply with production cuts agreement and increasing shale production	🔴	🔴	Short to medium term
Slowdown in key economies	• Slowdown in economies with strong trade relations with Nigeria, particularly China, the UK , the US and India	🟡	🟢	Short to Medium term
Monetary policy normalization	• Ongoing monetary policy normalization in the US could lead to a reversal of foreign capital and restrict further flows	🔴	🔴	
High inflation	• Pre-election and 2018 budget spending	🔴	🔴	Short to Medium term
	• Adjustment of petrol prices and power tariff	🔴	🟢	
Oil production disruption	• Attacks on oil and gas facilities by militant groups in the Niger Delta region	🔴	🟡	Short to Medium
Political risk/Heightened insecurity	• Pre-election uncertainties could elevate political tensions, and leadership succession could hamper policy continuity	🔴	🟡	Medium term
	• Continuous insurgency in the Northern region	🔴	🟡	Short to Medium term

🟢 Low 🟡 Medium 🔴 High

Abbreviations

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

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Thank you