

Snapshot of the Nigerian Macroeconomic Environment in 2021





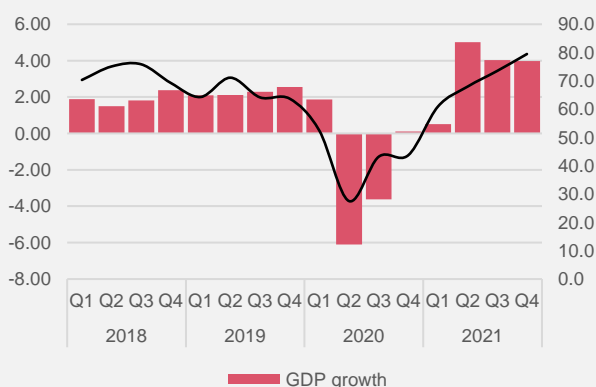
Disclaimer

Please note that in this bulletin we use the official statistics issued by the National Bureau of Statistics. These are issued to 3 or in some cases 4 (e.g., inflation) significant digits. In an economy where more than 50% of the economic activity is in the informal sector, it is difficult to estimate to this number of significant digits. However, at PwC Nigeria we have taken the position to use the official numbers for our reports, albeit to a single decimal point or the nearest whole number.

Nigeria's economic growth amidst the pandemic challenges

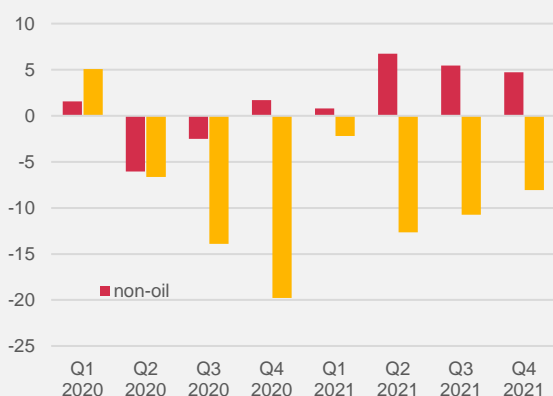
The Nigerian economy continues to sustain its growth momentum as **GDP expanded by 3.98% year-on-year in Q3 2021**. Consequently, Nigeria's real GDP growth stood at 3.4% in full year (FY) 2021, the strongest growth since 2014 when GDP growth was about 6.3%. This stellar performance was largely due to several factors including a positive base effect and more effective management of the pandemic.

Nigeria's quarterly real GDP growth rate (%) vs. average price of Bonny Light



Source: NBS, OPEC, PwC analysis

Oil vs non-oil sector growth rates (%)



Source: NBS, OPEC, PwC analysis

The non-oil sector grew by 4.7% in Q4 2021 compared to 5.4% recorded in Q3 2021 and 1.7% in Q4 2020. Non-oil sector growth in full year (FY) 2021 stood at 4.4% compared to the contraction of -1.3% recorded in FY 2020.

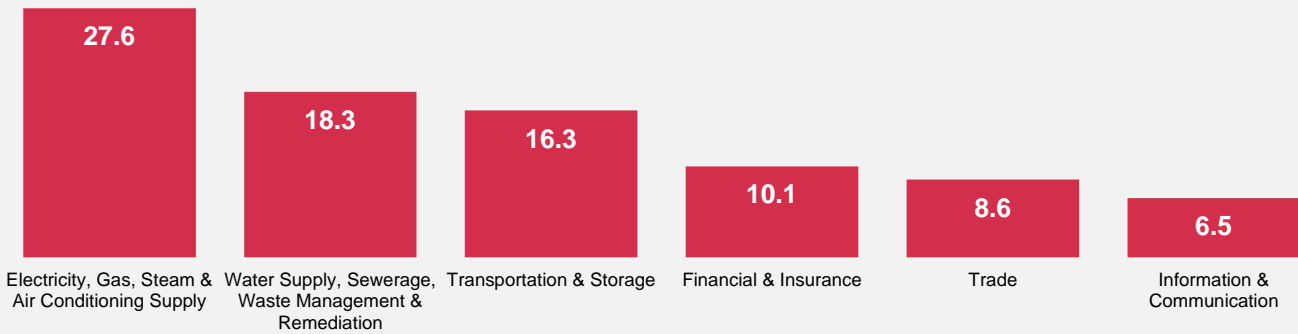
Meanwhile, the oil sector remains stuck in negative territory contracting by -8.1% in Q4 2021 which is slightly lower than -10.7% contraction posted in Q3 2021. The current decline marked the seventh consecutive quarterly contraction of the sector since the pandemic weighed negatively on the economy in Q2 2020. Consequently, oil sector growth sank by -8.3% in full year (FY) 2021 relative to 8.9% posted in FY 2020. While positive sentiments in the global crude oil market drove oil price to pre-pandemic level, the gain from the oil price rally, which averaged US\$70.5 per barrel in 2021 according to confirmatory data from OPEC, was lost by the continuous decline in domestic crude oil production. In 2021, domestic crude oil production averaged 1.6 million barrels per day (mbpd), a significant reduction compared to the average pre-pandemic and pandemic levels of 2.01 mbpd and 1.85 mbpd, respectively.



Fastest growing sectors in Nigeria in 2021

The top five fastest-growing sectors in 2021 were the electricity, gas, steam, and air conditioning supply (27.6%), water supply, sewerage, waste management and remediation (18.3%), transportation and storage (16.3%), financial and insurance sector (10.1%) and trade (8.6%). These five sectors accounted for about 21.3% of total GDP in 2021.

Nigeria's fastest growing economic sectors (%), 2021



Source: NBS, OPEC, PwC analysis

Recommendations

We believe that the government can fast-track Nigeria's economic growth by stimulating activities in the three key sectors – agriculture, services export, and telecommunication. A concerted effort by the Federal Governments (including state governments) and the CBN to synchronise fiscal and monetary policies towards eradicating the impediments hampering the performance of these sectors. We chose these sectors because of three key factors:

- the ability of these three sectors to create jobs for millions of Nigerians.
- the power these sectors hold in catalysing activities in other sectors including MSMEs and;
- the ability to stand as buffers in case of externally induced shocks such as the COVID-19 pandemic.

Nigeria's services export grew at an average of 16% over the past six years from US\$3.2 billion in 2015 to nearly US\$4 billion in 2020, driven primarily by selected services segments like transportation, financial and government services. In 2020, inflow from the export of transportation services stood at about US\$2.1 billion, representing more than half of the total size of the services export in the period under review.

The driver for the growth of services export is an increase in technological adoption capable of powering the conduct of businesses across borders in a seamless manner.

Nigeria's monetary policy direction in 2021

At the start of the year, the Nigerian economy was reeling from the pandemic's adverse effect, which exacerbated worsening economic conditions such as rising inflation, slow growth, declining reserves, exchange rate instability, etc. Due to the problem of a rising inflation rate and the slow growth of the GDP, the MPC committee decided to hold all monetary policy parameters constant all through the year.

Consequently, the CBN adopted (and in some cases deepened the implementation of) unorthodox monetary policies to change the negative trajectory of macroeconomic indicators like GDP growth, exchange rate and external reserves. Some examples of the policies deployed include Targeted Credit Facility (TCF), Anchor Borrowers' Programme (ABP), the eNaira, the Naira4dollar scheme, etc.

Below is a further breakdown of the CBN's policies' impact on the interest rate, exchange rate, and foreign reserves.

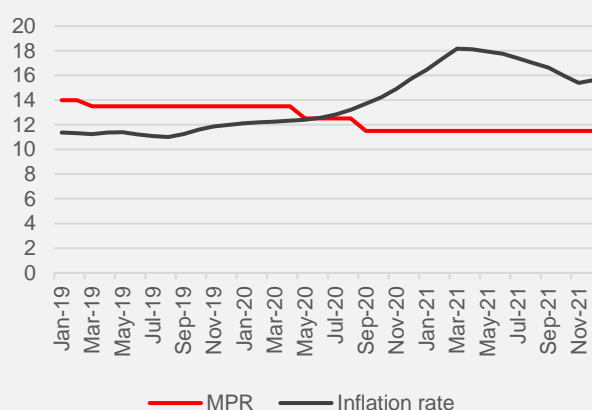
Interest rate

In 2020, central banks globally including, the Federal Reserves, European Central Bank and Bank of England, reduced interest rates via bond purchases. This approach, technically referred to as quantitative easing, was to spur growth because of the negative impact of the pandemic on the economy. Similarly, in Nigeria, the CBN reduced its monetary policy rate twice in 2020 before settling at 11.5%.

Unfortunately, most economies are struggling with the adverse effect of adopting quantitative easing amid a pandemic-induced supply chain disruption. Further, the quest for decarbonisation and global economic recovery has prompted the recent energy crisis, leading to soaring energy prices. The rise in inflation has forced some central banks to tighten monetary policy to prevent inflation from skyrocketing, e.g., the Federal Reserve announced that it would reduce bond purchases by \$15 billion monthly.

Fortunately for the Nigerian apex bank, the Nigerian economy seems to be temporarily immune from the rising global inflation rate that has hit most advanced and emerging economies, plus the fact that domestic headline, core, and food inflation have decelerated over the past seven months. The consecutive decline in inflation rate and the GDP growth propelled the CBN to maintain the status quo in its MPC meetings all through 2021.

Nigeria's quarterly real GDP growth rate (%) vs. average price of Bonny Light



Source: NBS, PwC analysis

Nevertheless, risks such as the emergence of new COVID-19 variants (Omicron variant), energy crisis, a slowdown in global economic activities, supply chain bottlenecks, and continued increase in domestic insecurity rate might change the dynamics of the Central Bank's monetary policy rate in the future.

At approximately 16%, Nigeria's inflation rate is high. Due to global and domestic risk factors, an upsurge in the inflation rate might force the CBN to tighten its monetary policy stance. On the other hand, the continuous decline in the inflation rate might create headroom for the CBN to marginally ease the monetary policy rate to strengthen economic growth further.

Foreign Reserves

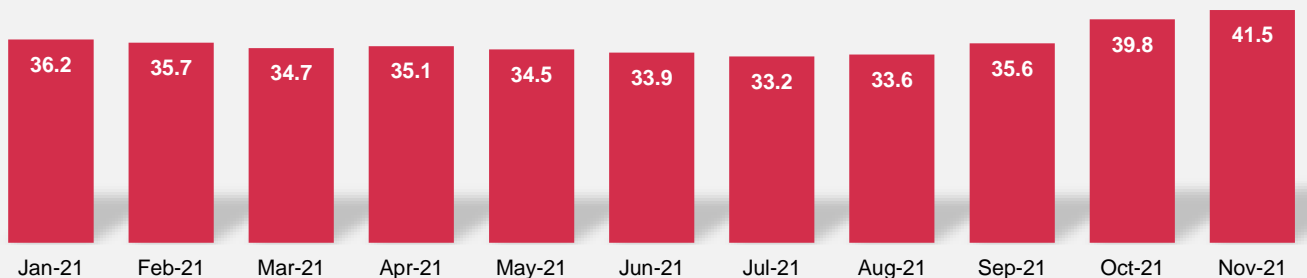
Nigeria's foreign reserves hit the \$40 billion mark in 2021 for the first time since 2019. The rise in the reserves could be attributed partly to the successful \$4 billion Eurobond issue, increased oil price, and the \$3.3 billion SDR allocation from the IMF. Despite the improvement, Nigeria's foreign reserve position remains significantly vulnerable to changes in oil price.

The high demand for dollars and the consistent intervention of the CBN in the foreign exchange market has put significant pressure on Nigeria's foreign reserve position. A major fundamental way to boost Nigeria's foreign reserves would be to

attract more capital importation, especially FDI, which is more permanent, boost competitive non-oil export, etc.

Most recent statistics from the NBS in Q3 2021 revealed that Nigeria's import value stood at N8.2trn while the value of its exports stood at N5.1 billion, signifying a negative trade balance of N3 trillion in Q3 2021. Volatile crude oil exports accounted significantly for 78.5% of total exports to further compound the woes. Boosting non-oil export is pivotal as global trends reveal that countries with the highest foreign reserves, such as China, Japan, Switzerland, export more than they import.

Nigeria's foreign reserves 2021 YTD (US\$'bn)



Source: NBS, PwC analysis

In Q2 2021, Nigeria's capital importation stood at \$875.6 million, representing a decline of -32.3% compared with Q2 2020. But the performance of Nigeria's FDI inflow has been abysmal in 2021. Data from the NBS reveals that Nigeria's FDI as of Q2 2021 stood at \$77 million, the lowest quarterly inflow since Q1 2014.

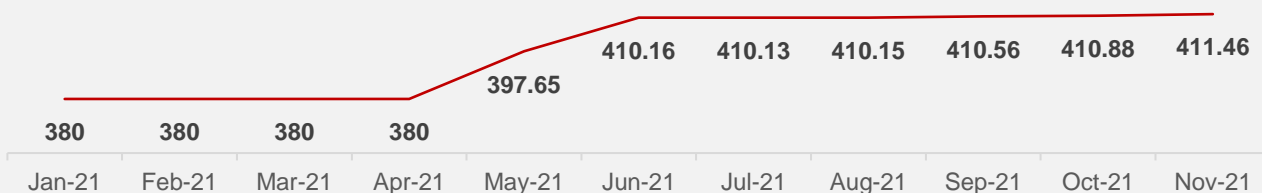
To shore up foreign reserves and boost its capital account, the government should break state-owned monopolies that shut foreign investment out. Doing this will attract the foreign investment needed to fix infrastructure decay. It can be implemented in several ways including, immediate IPOs on existing state-

owned enterprises, increasing the issuance of new licenses for greenfield projects, and engaging the world about the future of Nigeria's economy through all the ministries, departments and agencies, diplomatic outlets, etc.

Exchange rate

In May 2021, the CBN adopted the NAFEX rate as its official exchange rate, depreciating the naira by 7.6% to about N407.8/\$ from its previously fixed rate of N379/\$. Adopting the NAFEX rate was a commendable step towards unifying the exchange rate, which is in line with the positions of many economic experts and international bodies, like the IMF.

Nigeria's exchange rate (N/US\$)



Source: NBS, PwC analysis

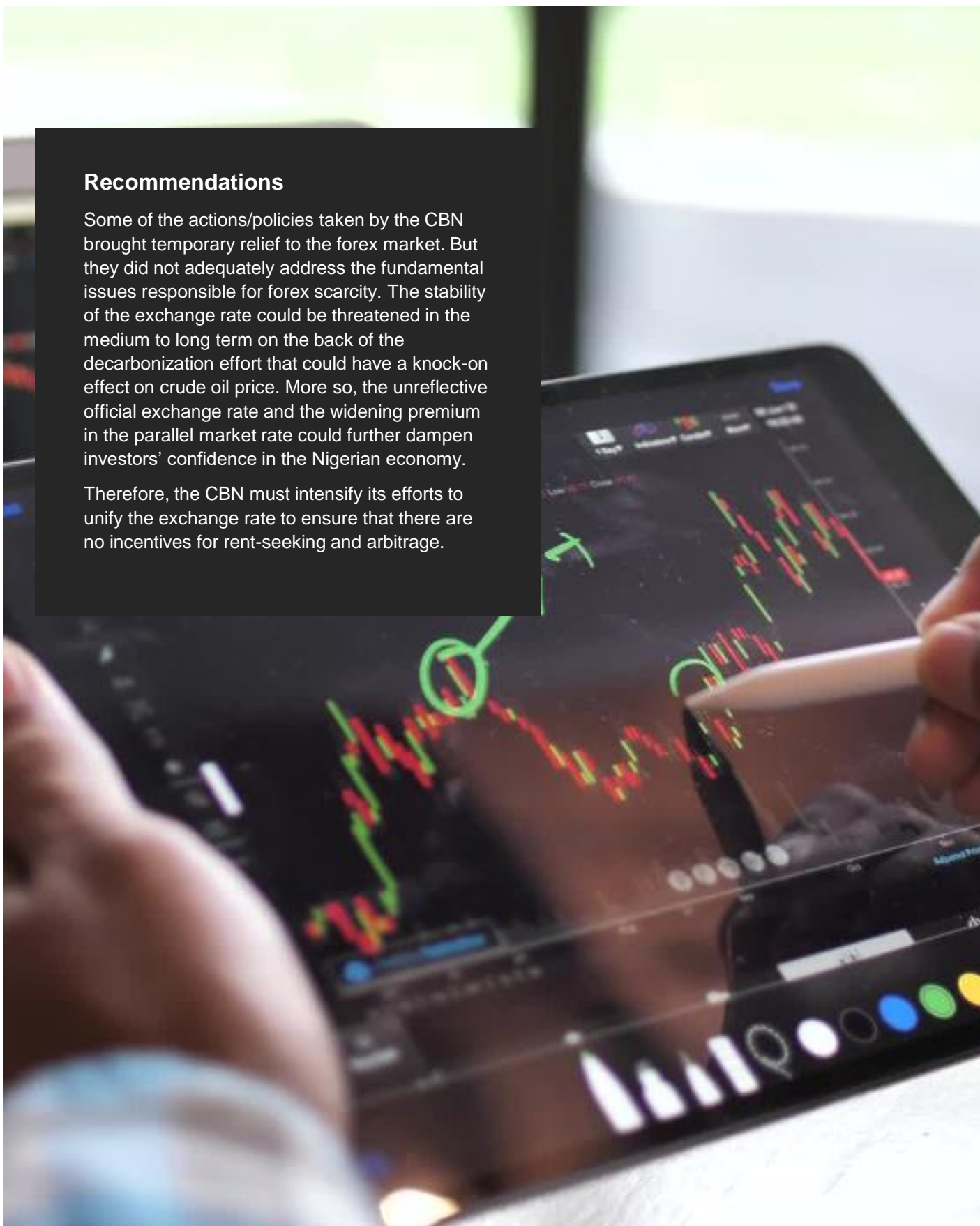
The CBN introduced several policies in 2021 to reduce the demand pressure on the naira and prevent the continuous depreciation of the naira.

Some of these policies include the instruction to banks to transfer all diaspora remittances to the domiciliary accounts of the beneficiaries or payment to the customers in foreign currency, naira for dollar scheme, banning sales of forex to BDCs etc.

Recommendations

Some of the actions/policies taken by the CBN brought temporary relief to the forex market. But they did not adequately address the fundamental issues responsible for forex scarcity. The stability of the exchange rate could be threatened in the medium to long term on the back of the decarbonization effort that could have a knock-on effect on crude oil price. More so, the unreflective official exchange rate and the widening premium in the parallel market rate could further dampen investors' confidence in the Nigerian economy.

Therefore, the CBN must intensify its efforts to unify the exchange rate to ensure that there are no incentives for rent-seeking and arbitrage.

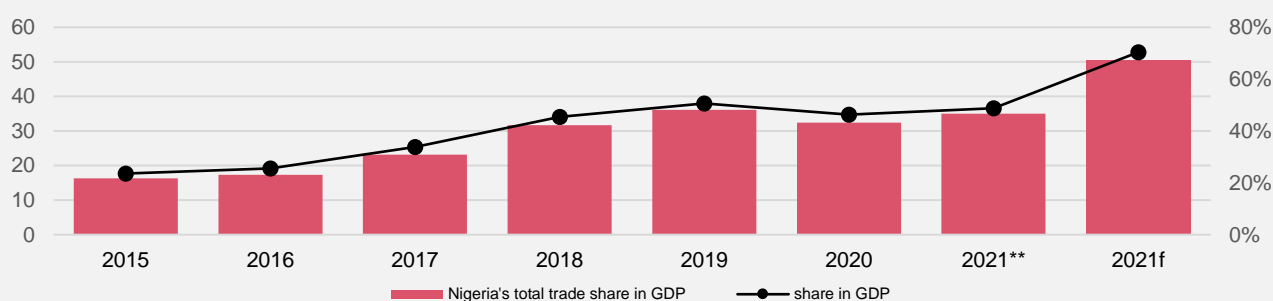


Nigeria's current external trade position threatens economic stability

In the year under review, aggregate trade rose by 10.4% and 58.6% year-on-year to N13.3 trillion in Q3'2021 from N12 trillion and N8.4 trillion recorded in Q3'2020 and Q2'2021, respectively. Nigeria's cumulative trade stood at over N35 trillion by the

end of the third quarter (Q3) 2021, representing nearly half of the real GDP. Nigeria's total trade could rise above N50 trillion by the end of 2021 (representing about 70% of real GDP) if the current quarterly growth trend continues, all things being equal.

Nigeria's total trade (N' trillions)



Source: NBS, PwC analysis f – forecast ** figure is as at nine months (9M) 2021

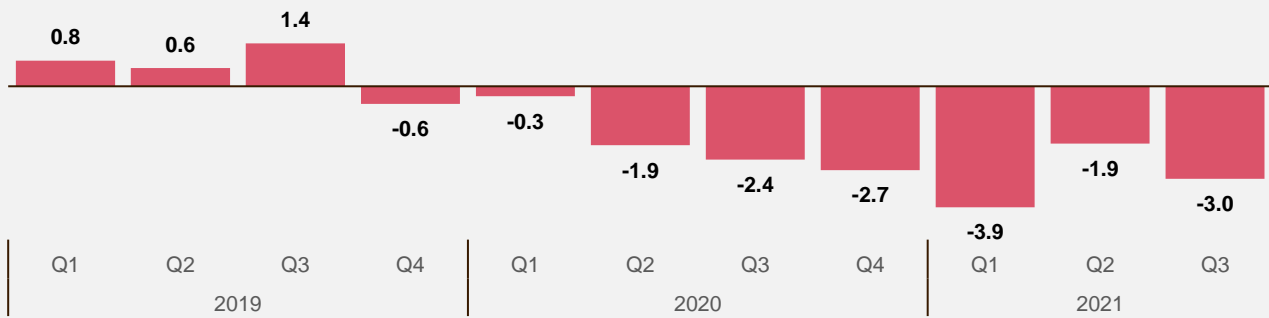
The high trade value is attributable to the increasing rate of imports, which contributes about 61.4% to the total trade position in Q3 2021. Nigeria's import year-to-date stands at over N21.9 trillion as of Q3 2021. Essential import items like machinery and transport equipment, mineral fuel, chemicals, and other related products accounted for about two-thirds (69%) of the total import value in Q3 2021.

Meanwhile, the country's export position remains driven by crude oil export within the period under review despite the volatile global crude oil price. The recent rally in crude oil price fueled by increased international economic activities has helped to stimulate domestic export. Crude oil export accounted for 78.5% of the total export value of N5.1 trillion recorded in Q3 2021. Non-oil export remains subdued on the back of the country's uncompetitive manufacturing sector that has been inhibited by FX liquidity crunch, FDI drought,

insecurity, poor value addition etc. Still, Nigeria's cumulative export value between Q1 - Q3 2021 rose to N13.1 trillion compared to N9.3 trillion in the same period last year.

More worrisome is the continuous trend of the country's external trade imbalance following the aftermath of the land border closure by the government in Q3 2019 as part of efforts to curb smuggling and boost local production capacity. The gap between Nigeria's imports and exports worsened with the pandemic outbreak, increasing from N1.9 trillion to nearly N4 trillion by Q1 2021. The trade balance has widened significantly despite the recent oil price rally. By the end of Q3 2021, the trade deficit had expanded by over N3 trillion, substantially higher than the N1.9 trillion recorded in Q2 2021.

Nigeria's external trade balance (N' trillions)



Source: NBS, PwC analysis

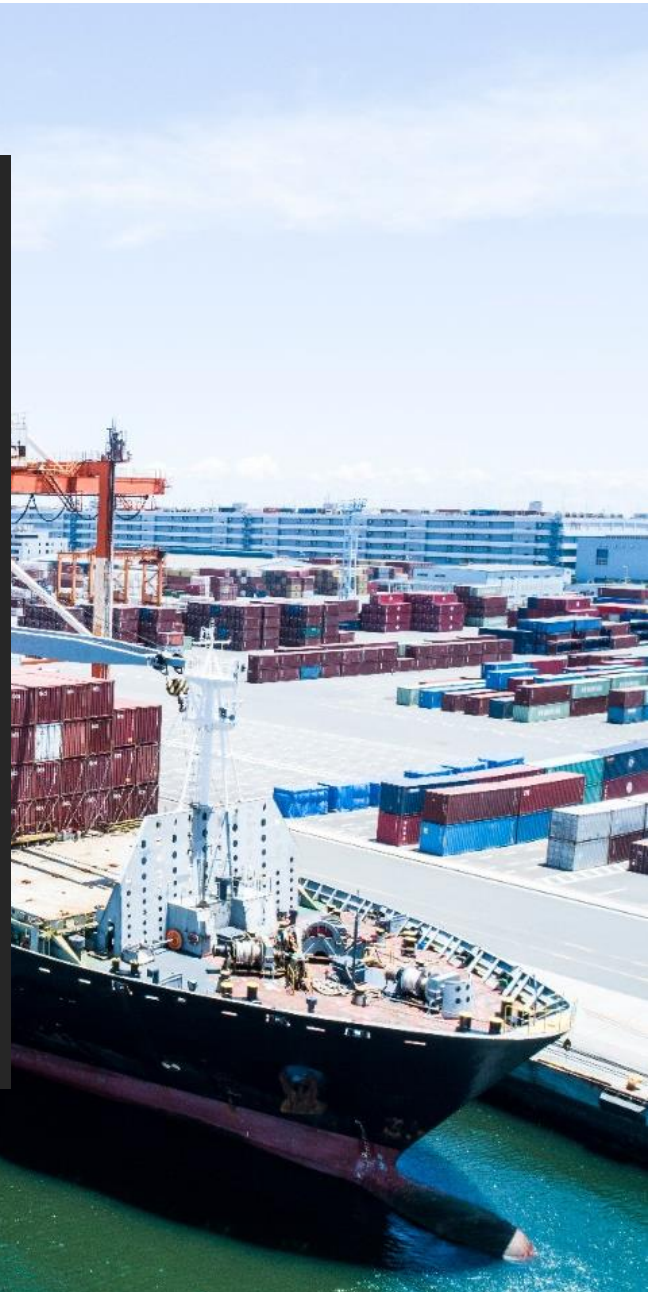
Receipts from international trade account for a significant portion of the nation's external reserve. Consequently, the continuous increase in the

nation's trade deficit could worsen the foreign exchange reserve position and impede the ability of the CBN to intervene in the forex market to stabilize the naira.

Recommendation

There is a need to broaden the export base of Nigeria away from crude oil. The African Continental Free Trade Area (AfCFTA) can help Nigeria achieve this. The AfCFTA, which came into effect on the 1st January 2021, creates a single market for goods and services across 54 African countries. The agreement sets the conditions for the free movement of persons, investments, and a customs union to streamline trade in Africa for Africa's economic integration and prosperity.

Nigeria can leverage its position as the largest economy in Africa to exploit the advantage that AfCFTA holds. It can do this by creating business expansion opportunities in terms of the number of business branches and supply chains (e.g., the manufacturing and agricultural sectors). Nigeria can also exploit its vast population, as nationals can source job opportunities locally and within the trade area, attracting more remittance inflows to Nigeria.

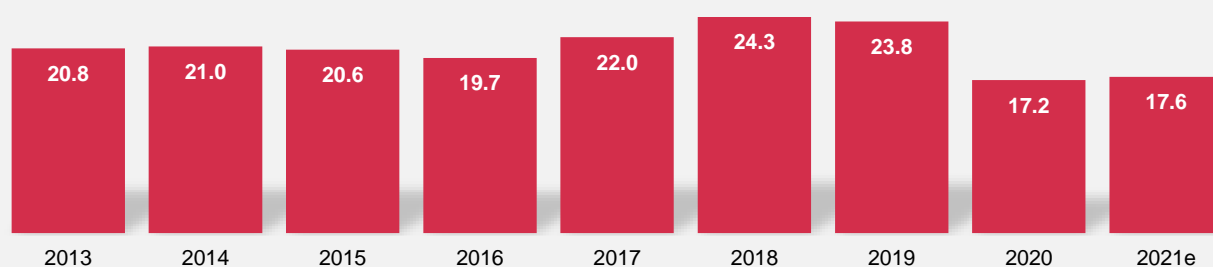


The resilience of diaspora remittances

Nigeria dominates remittance inflow into Sub-Saharan Africa (SSA) given the country's large diaspora. Following the COVID-19 pandemic,

Nigeria's remittance inflows declined by 28% (US\$6.6 billion) to US\$17.2 billion in 2020 from US\$23.8 billion recorded in 2019.¹

Nigeria's diaspora remittance inflows (US\$ million)



Source: World Bank, PwC analysis

The lackluster performance of Nigeria's diaspora remittance crept surreptitiously into 2021. In Q1'2021, remittance inflows fell by 24% to US\$4.2 billion from US\$5.6 billion recorded in the corresponding period of the previous year.² By first half (H1) 2021, official data reveals a jump in diaspora remittance value by 15.5% to US\$9.2 billion (H1 2020: US\$7.98 billion) driven by efforts by the CBN to channel inflow through the domestic banking system by leveraging the Naira4dollar scheme. As the Nigerian diaspora continue to increase, so will remittances. The World Bank projects Nigeria's diaspora remittance inflow to hit US\$17.6 billion by the end of 2021, representing a marginal increase of 2.3% over its value in 2020, albeit still below the average pre-pandemic level of US\$23 billion.

In H1 2021, the value of diaspora remittance was significantly higher than the FDI inflow, demonstrating the resilient nature of migrant remittances amid the pandemic. With the rising trade deficit and likely decline in crude oil price in the wake of the outbreak of the Omicron variant of COVID-19, diaspora remittance could well be the lever that authorities could pull to support the forex reserve and stabilize the exchange rate.



1. Information is according to data from the World Bank
2. <https://nairametrics.com/2021/09/06/diaspora-remittances-into-nigeria-fall-by-24-in-q1-2021/>



Recommendation

The Naira4dollar scheme incentivised people to use the formal system to channel their remittance into the country. But there is still a significant portion of the informal remittance market outside the authorities' control, partly due to the exorbitant cost of sending money to the country using formal channels. The cost of remittances into Nigeria, which is about 8.9% of US\$200, is still relatively high compared to countries such as India (5.4%), Ghana (7.4%) and Egypt (4.9%).

Consequently, Nigeria can scale up its remittance inflows by encouraging the use of digital technologies in the entire remittance value chain. This will help to stimulate competition in the space that will reduce the average transaction cost of sending remittances, formalize the informal remittance space and cut the long waiting time between when money is sent and when it is eventually received.

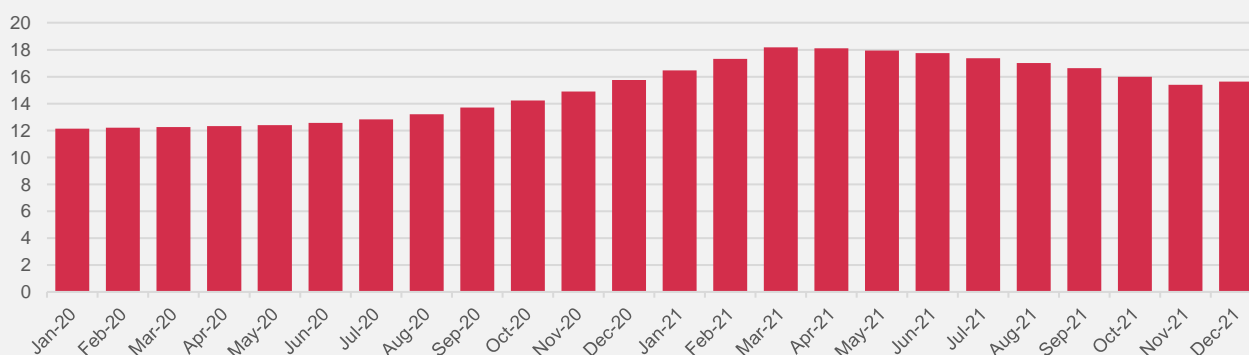
Part of digitizing the remittance space will also involve reviewing the existing regulatory structure that inhibits the deployment of technology to ease transaction initiation, processing, and disbursement.

Inflation rate in Nigeria

The inflation rate has exhibited mixed trend over the past few months, increasing from 12.13% in January 2020 before peaking at 18.17% by the end of March 2021. However, the inflation rate

decelerated consecutively from 18.12% in April 2021 to 15.39% in November 2021 which is higher than the CBN target of between 6–9% and the target of 13% set by the FG in the 2022 budget.

Headline inflation rate in Nigeria (%)

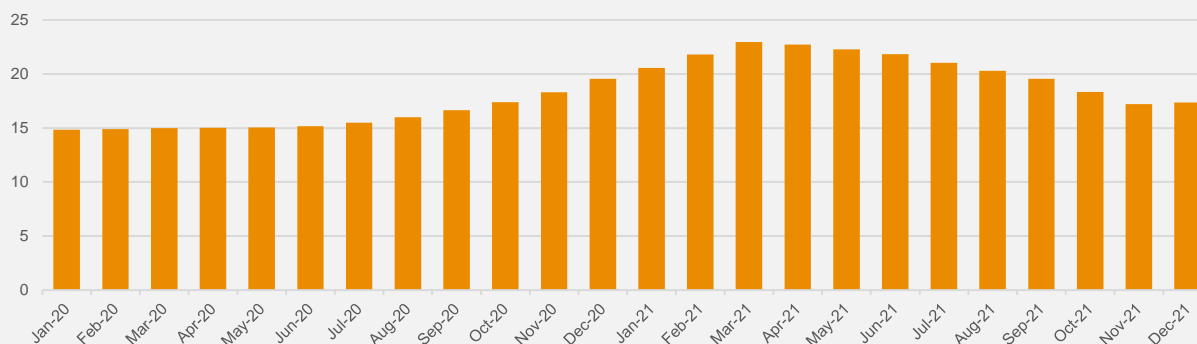


Source: World Bank, PwC analysis

Food inflation has decelerated consistently over the past six months, from 22.95% in March 2021 to 18.34% by October 2021. The sustained economic activities at the festive season caused food prices to shoot up marginally in December 2021 to 17.37% 17.21% in November 2021. But the current rate remains relatively high and could derail the gain

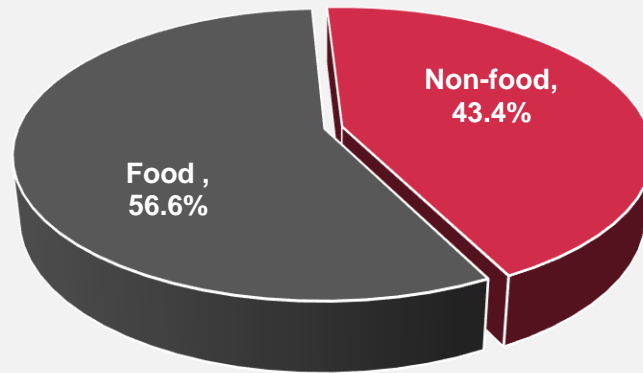
already recorded in the fight against poverty and socio-economic inequality in the country. This is because Nigerians spend a substantial sum of their total expenditure on food. According to official data, Nigerians spent about N22.8 trillion on food in 2019, representing about 57% of total consumption expenditure for that year.

Food inflation rate in Nigeria (%)



Source: NBS, PwC analysis

Share of total food and non-food items in aggregate consumption expenditure, 2019



Source: NBS, PwC analysis

Key growth drivers of inflation in Nigeria

The inflationary trend in Nigeria is unusual and is driven predominantly by both supply-side factors and demand-side shocks. Consequently, attempts at taming the spiralling trend will require an in-depth understanding of these factors.



Widespread insecurity across the country leading to reduction in food production



Distortions in the foreign exchange market as well as the CBN's FX restriction policy for 40 items



Poor infrastructure which creates unnecessary cost for manufacturers, farmers, suppliers and traders.



Emerging threat of climate change to food production.

The effect of the inflation rate is evident in our daily lives. The inflation rate directly impacts private consumption capacity. Nigeria's increased inflation rate has led to a drastic reduction in the purchasing power of households. These households are experiencing a significant loss of real income and decreased living standards due to rising costs. The high inflation rate and the rising unemployment rate could further push many more Nigerians into poverty, especially in the face of stagnant and insufficient income for the lower-income group.

The inflation rate also poses a significant economic headache to CBN due to its effect on the value of the domestic currency, interest rate and foreign investment.

A rising inflation rate necessitates raising the benchmark interest rate, which is essentially a monetary policy tool to rein in price fluctuations above or below the predetermined macroprudential level. But the CBN has since shifted its monetary policy stance away from inflation to targeting boosting economic growth. The apex bank believes that Nigeria's inflation rate is due to structural rigidities. And that this could best be tackled by increasing domestic output and boosting the resilience of growth-enhancing sectors that will eventually lower inflationary pressures.

Recommendations

Authorities need a multipronged approach to curb the scourge of inflation in Nigeria. There is a need to unify the foreign exchange rates and tackle widespread insecurity and the challenges of weak legacy infrastructure. Doing this will drastically reduce the inflation rate, especially food prices. Through a PPP framework, the government can unlock private financing for infrastructure projects to enhance agricultural productivity and overall economic activities. This will help to stimulate fast delivery of agricultural commodities to the market, bring down the cost of production and reduce unnecessary wastages and inefficiencies along the domestic supply chain.

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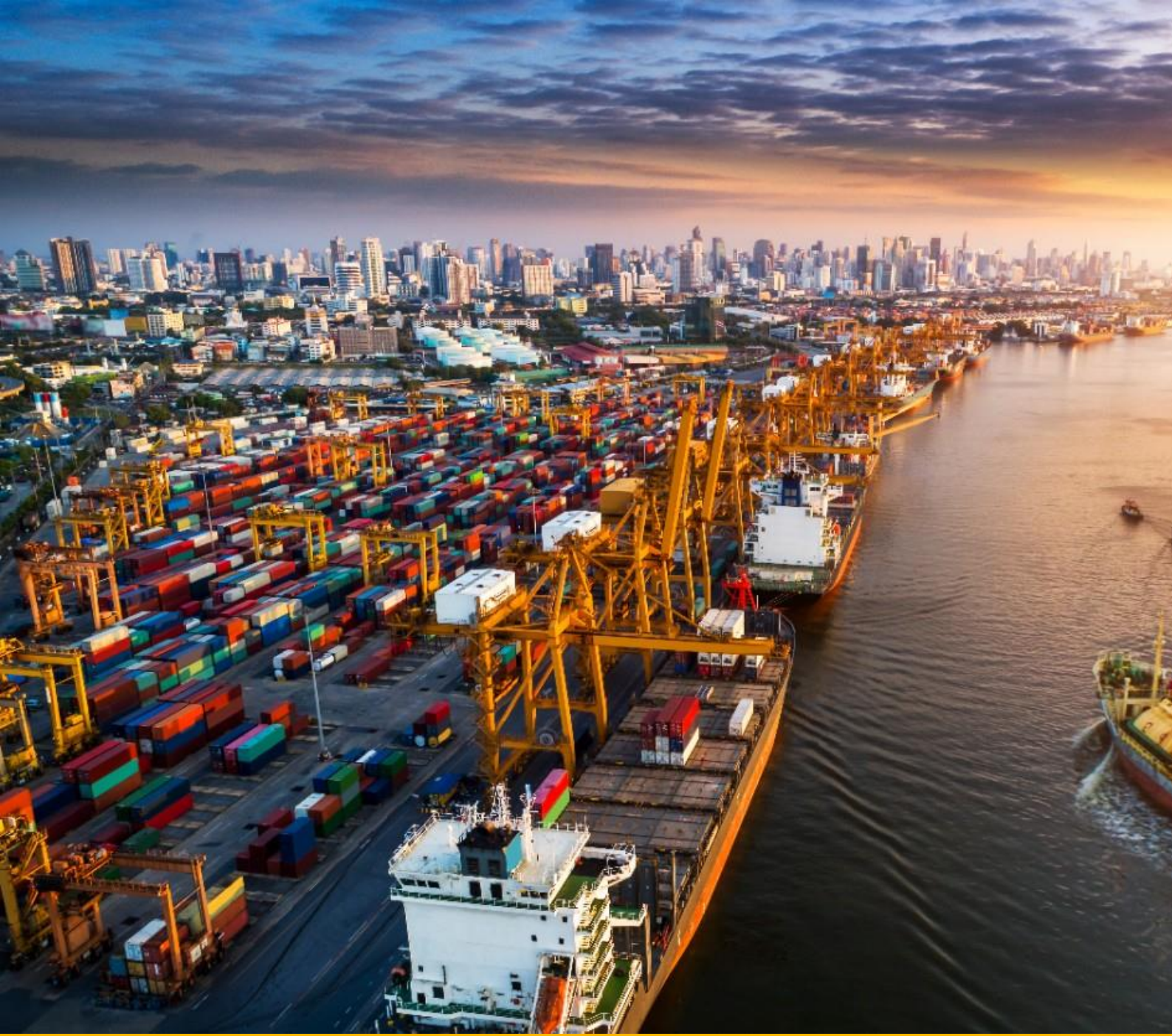
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