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Berkshire Market Briefs

Q1 2024 Quarterly Report - Key Economic Indicators and Markets – Review, Outlook & Implications

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Executive Summary

Over the past 14 quarters, the Nigerian economy has maintained a growth trend, achieving an average growth rate of 2.85%. Specifically, in Q1 2024, the economy expanded by 2.98%, a slight decrease from 3.46% in the previous quarter. While the ongoing growth trend is commendable, the slower pace of growth largely reflects enduring challenges in the real sector. Factors such as the significant depreciation of the Naira, increased insecurity, diminished purchasing power, and assertive monetary tightening measures by the Central Bank of Nigeria (CBN) have all hampered economic growth and impeded overall development.

Inflation has remained a hydra-headed problem in Nigeria like in most developing nations. Headline inflation, which measures the year-on-year change in the general price level has been increasing steadily since January 2023, climbing to a 28-year high of 33.95% in May 2024 due to both monetary and structural factors. While the CBN has been aggressive in using its traditional monetary tools to rein in inflation and restore confidence in the foreign exchange rate market, there is a need for complementary efforts from the fiscal authorities to address the underlying structural challenges and increase the effectiveness of monetary policy. The good news is that the harvest season is expected to kick-start in the third quarter, which implies that commodity supply is likely to increase, reducing the pressure on prices. Hence, headline inflation could peak and start declining.

Apart from targeting inflation, the CBN's aggressive rate hike and forex reforms have boosted foreign portfolio investors' participation in Nigerian securities, increasing dollar inflows and strengthening the Naira. Consequently, the currency appreciated to ₦1,055/$ (a six-month high) in the parallel market at the beginning of the quarter before depreciating again towards the end of the quarter. Currency weakness is likely to persist in the near term because of the summer season. However, the $2.25 billion World Bank loan will offer temporary support to the currency.

The banking sector was confronted with significant liquidity challenges due to the CBN's mopping-up exercise and the high yield in the fixed-income market. The stock market also recorded a bearish performance as the NGX ASI lost 4.31% to close at 100,057.49 points on June 28 from 104,562.06 points on March 28.

Total trade spiked 46.27% to N31.81 trillion in Q1'24, largely due to currency depreciation

In the first quarter of 2024, Nigeria's total trade surged by 46.27% to ₦31.81 trillion in nominal terms but decreased by 8.72% to $23.77 billion in dollar terms. Both export earnings and import costs followed a similar pattern. Total export value increased sharply by 51.06% to ₦19.17 trillion in nominal terms but declined by 5.79% to $14.32 billion in dollar terms. Similarly, the total import bill rose by 39.67% to ₦12.64 trillion nominally but fell by 12.82% to $9.45 billion in dollar terms. Importantly, there was a significant rise in the nominal trade surplus by 79.12% to ₦6.52 trillion, while in dollar terms, it saw a slight increase of 11.7% to $4.87 billion.

Nigerian commodities were predominantly exported to Europe, led by France at 11.09%, followed by Spain (10.56%), The Netherlands (8.85%), India (8.41%), and the United States (6.84%). These five countries accounted for 45.75% of total export proceeds. Crude oil remained the primary export commodity, representing 80.80% (₦15.49 trillion) of total export earnings, followed by natural gas (8.75%, ₦1.68 trillion), and sesame seeds (₦0.25 trillion, 1.29%).

China (23.18%), India (8.46%), the United States (7.98%), Belgium (7.56%), and the Netherlands (4.68%), were the leading importing countries, collectively representing 51.86% of total imports. The most imported commodities included Motor spirit ordinary (₦2.63 trillion, 20.84%), gas oil (₦1.20 trillion, 9.46%), and Durum wheat (₦0.52 trillion, 4.11%).

Outlook and Implications

The wider trade surplus is positive for Nigeria's economy as it can strengthen gross external reserves and improve the Central Bank's capacity to support the Naira. Nonetheless, the disparity between nominal and dollar-based trade figures highlights the country's susceptibility to currency fluctuations. More disturbing is the fact that real export earnings decreased despite the weakened Naira. This points to fundamental challenges within the export sector, limiting Nigeria's ability to fully leverage the competitive benefits of a devalued currency.

Capital Importation Spikes 210.16% to $3.38 billion in Q1 2024

Total capital inflows into Nigeria amounted to $3.38 billion in the first quarter of 2024, marking a significant rise of 210.16% compared to $1.09 billion in Q4 2023 and a 198.06% increase from $1.13 billion in Q1 2023. This substantial increase largely reflects renewed confidence in Nigeria's economy, driven by recent reforms implemented by the current administration. Portfolio investment constituted the largest portion of total capital imports (61.48%), followed by other investments (34.99%) and foreign direct investment (3.53%). Notably, foreign direct investment saw a decline of 35.22% to $119.18 million from $183.97 million in Q4 2023, while portfolio investment and other investments surged by 571.49% and 98.4% to $2.08 billion and $1.18 billion, respectively. These figures underscore the impact of the Central Bank of Nigeria’s rate adjustments in attracting foreign investors to Nigerian financial assets. However, Nigeria's challenging business environment continues to deter foreign direct investment.

The primary sources of these inflows were the United Kingdom ($1.81 billion, accounting for 53.49% of the total), the Republic of South Africa ($582.34 million, 17.25%), and the Cayman Islands ($186.21 million, 5.52%). Lagos State remained the top destination, capturing 82.42% of total capital inflows ($2.78 billion), followed by Abuja with 17.58% ($593.58 million) and Ekiti State with a minimal share. This trend is unsurprising as both Lagos and Abuja are major economic hubs.

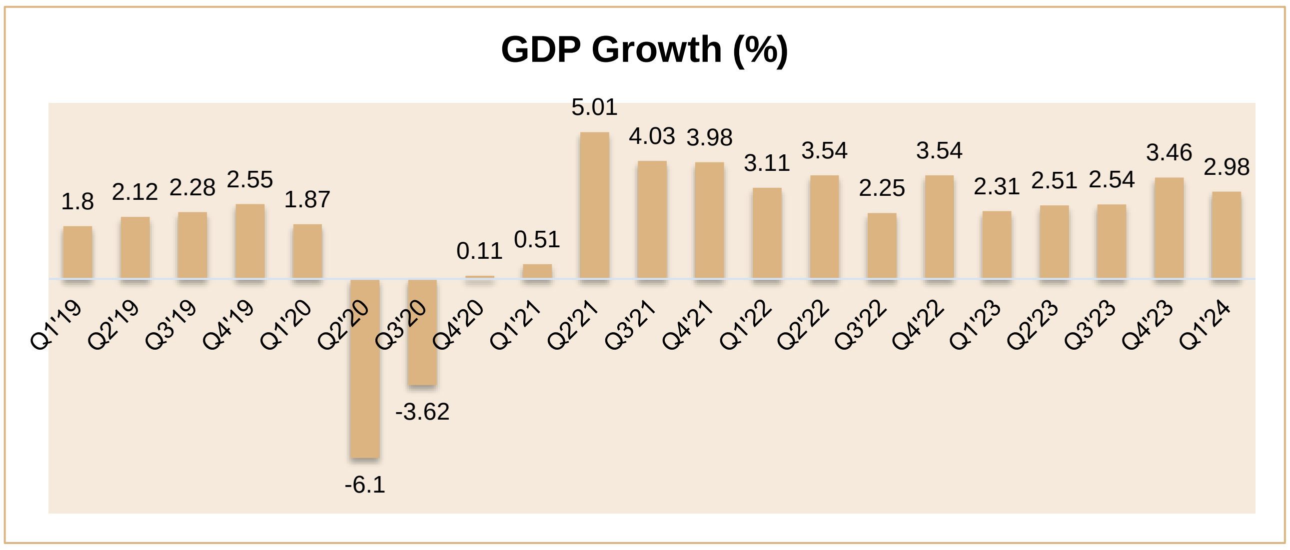
In terms of sectors, the banking sector attracted the highest capital inflow ($2.07 billion, 61.24%), followed by the trading sector ($494.93 million, 14.66%) and the production/manufacturing sector ($191.92 million, 5.68%). Stanbic IBTC Bank Plc received the largest amount of capital inflow during the period under review ($1.26 billion, 37.24%), followed by Citibank Nigeria Limited ($547.71 million, 16.22%) and Rand Merchant Bank Plc ($528.73 million, 15.66%).

Outlook and Implications

We anticipate a rise in foreign portfolio investment supported by the CBN's persistent robust monetary policies. Nevertheless, foreign direct investment is expected to continue its decline owing to the challenging business climate. Recent developments indicate a trend of multinational companies divesting from Nigeria, such as Diageo's sale of its 58.02% stake in Guinness Nigeria to Tolaram Group.

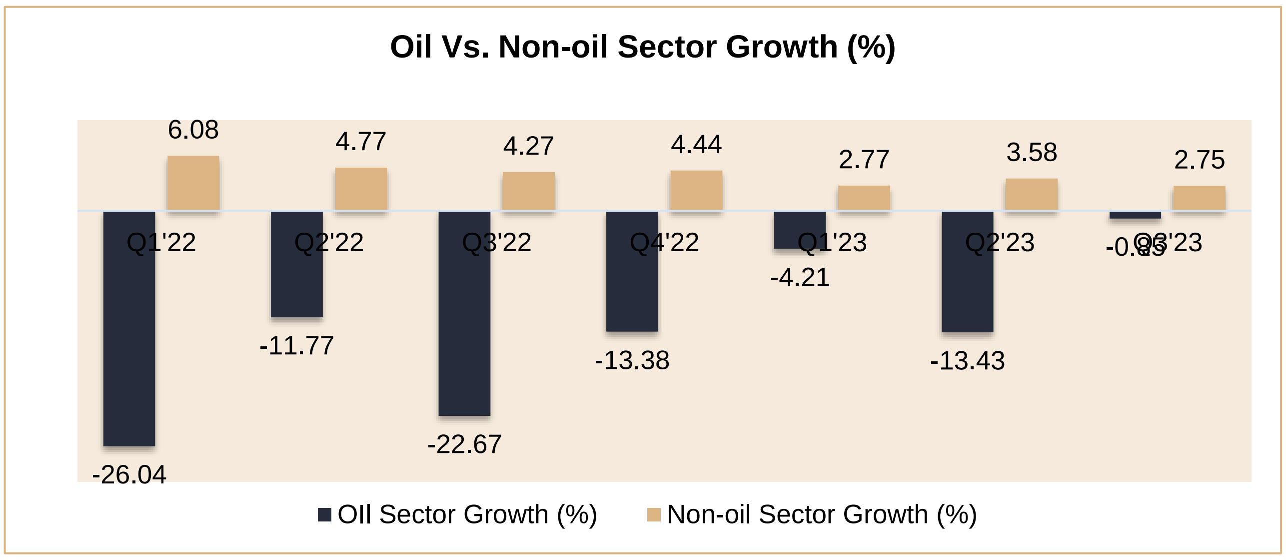
Real GDP Growth Sustains its Positive Trend but Moderates to 2.98% in Q1 2024

Nigeria's real GDP growth came in at 2.98% in Q1'24, a decline from 3.46% in Q4'23 but higher than the 2.31% recorded in Q1'23. This decline relative to the previous quarter was not surprising, given the typical slowdown in economic activities at the beginning of the year, exacerbated by the heightened insecurity, sharp Naira depreciation, weak aggregate demand, and the Central Bank of Nigeria's (CBN) hawkish monetary policy stance. The Naira reached a peak of ₦1,915/$ during the quarter, pushing up import costs and stifling business expansion. To mitigate inflationary and currency pressures, the CBN also implemented a series of interest rate hikes totalling 600 basis points in Q1'24, thereby elevating the cost of borrowing and further restraining business growth.



In the first quarter of 2024, there was a slowdown in both the oil and non-oil sector growth. The oil sector growth slowed to 5.70% from 12.11% in Q4'23, although it exceeded the negative growth rate of -4.21% observed in Q1'23. This slowdown was despite a rise in average oil production, suggesting that higher oil production was insufficient to compensate for the decline in prices. Oil production increased by 1.29% to 1.57 million barrels per day while oil prices dropped by 1.30% to $81.74 per barrel. Meanwhile, the oil sector's contribution to GDP rose to 6.38% from 4.6% in Q4'23 and 6.21% in Q1'23.

During the review period, the non-oil sector grew by 2.8%, a decline from 3.08% in Q4'23 but higher than the 2.78% in Q1'23. Expansion in this sector was fuelled by financial institutions, telecommunications, crop cultivation, trading, and the food, beverage, and tobacco industries. The non-oil sector contributed 93.62% to GDP in Q1'24, down from 95.30% in Q4'23 and 93.79% in Q1'23.



A breakdown of the NBS data showed that only 14 of the 46 activities tracked expanded, while 19 slowed and 13 contracted. Some of the sectors that slowed and contracted include:

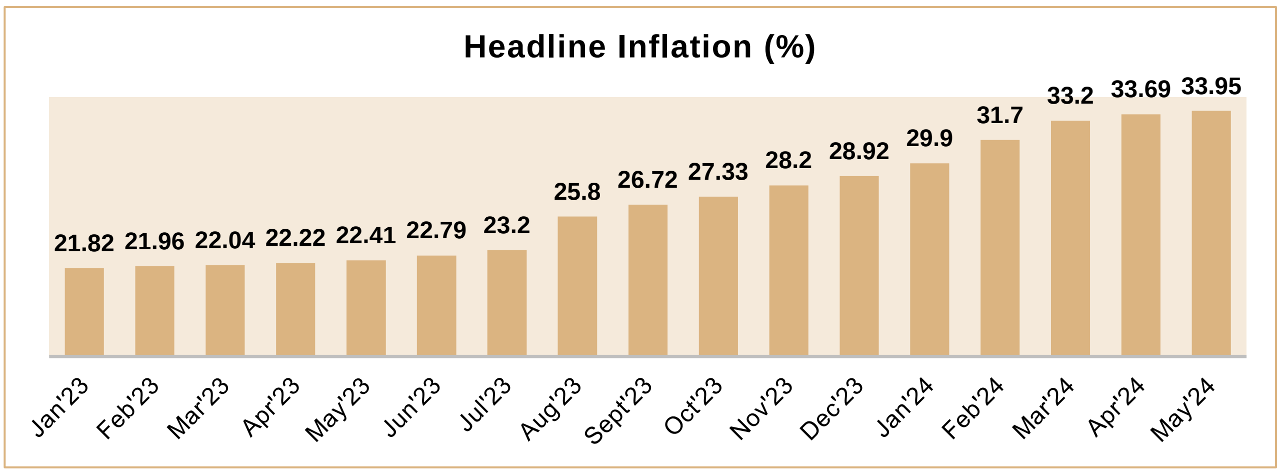
Sector	Q4'23	Q1'24	Rationale
Agriculture	2.10	0.18	▪ The sector was affected by insecurity challenges in the food belt, higher logistics costs, infrastructure deficiencies, and exchange rate pass-through
Trade	1.40	1.23	• Slowdown was partly due to weak demand and cost pressures emanating from currency depreciation
Construction	3.70	-2.14	• The sector was affected by subdued demand amidst rising costs of building materials

Outlook and Implications

We anticipate that real GDP growth will continue to be positive; however, it may further decline in the second quarter due to the lagged impact of significant currency depreciation and the Central Bank of Nigeria's (CBN) hawkish monetary stance. This situation could be aggravated by shortages in the agricultural sector during the second quarter, which coincides with the peak of the planting season.

Headline inflation maintained its upward trajectory in Q2'24

Inflation persisted through the second quarter, with headline inflation hitting a 28-year peak of 33.95% in May, up from 33.20% in March. However, the slope of the curve is flattening out, an indication that an inflection could be reached soon. This is further reinforced by the moderation in month-on-month inflation for the third consecutive month to 2.14% in May. The CBN has been aggressive in its fight against inflation, increasing the MPR by a cumulative of 750 basis points so far in 2024. However, Nigeria's inflation challenges are not solely due to monetary factors. Therefore, there is a critical need for complementary efforts from fiscal authorities to enhance the effectiveness of these monetary measures.

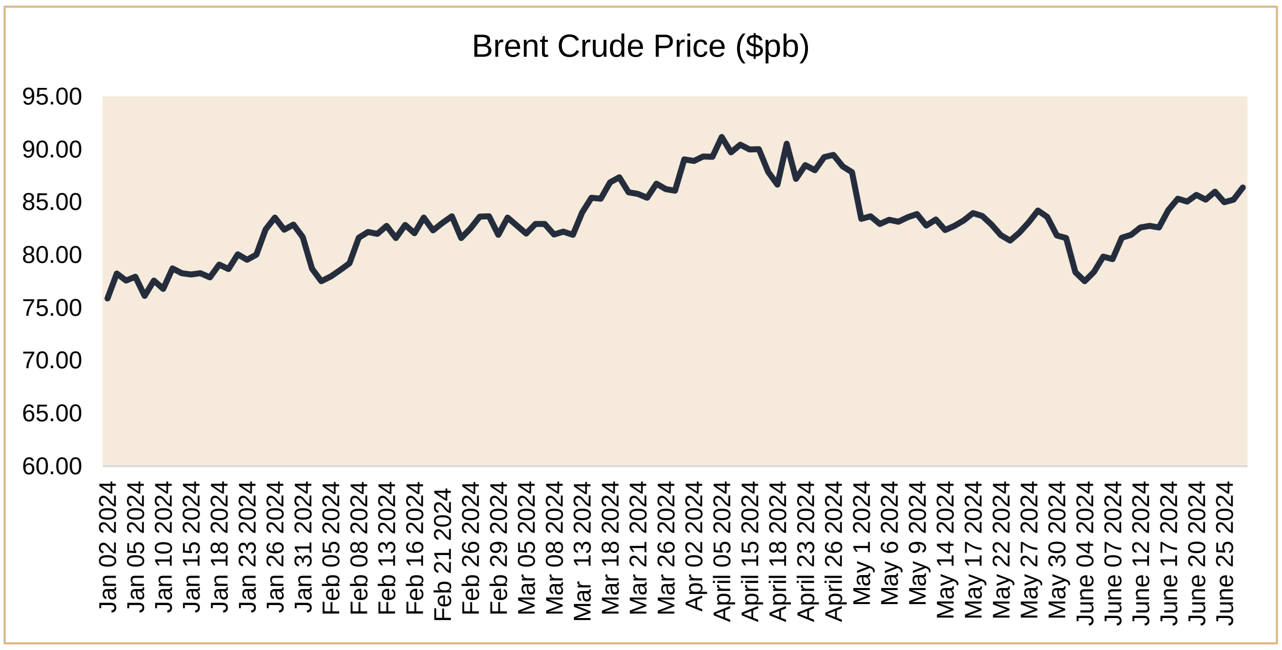


Outlook and Implications

We expect headline inflation to reach its highest point in June and then start to decrease in Q3 2024, supported by the Central Bank of Nigeria's continued aggressive monetary policy. The upcoming harvest season in the third quarter is also expected to contribute to a slowdown in price increases. However, a potential risk factor is the possibility of renewed foreign exchange pressure, given Nigeria's significant dependence on imports.

Oil Market – Geopolitical tensions and summer demand pushing up oil prices

On average, Brent crude price increased by 3.72% to $84.78 per barrel in the second quarter of 2024 from $81.74 per barrel in the first quarter. This rise was largely driven by growing expectations of interest rate cuts by the U.S. Federal Reserve, coupled with concerns over potential supply disruptions due to geopolitical tensions in Russia and the Middle East. Additionally, the anticipated surge in fuel demand during the peak summer season contributed further to the upward trend.



After three consecutive months of decline, domestic oil production rose by 5.19% to 1.42 million barrels per day in May. Although this is a positive development, it is important to note that Nigeria's production still falls below its OPEC quota of 1.58 million barrels per day and remains lower than the 2024 budget benchmark of 1.78 million barrels per day. On average, oil production decreased by 2.13% to 1.38 million barrels per day in Q2 2024 (April/May) from 1.41 million barrels per day in Q1 2024. Meanwhile, Nigeria maintained 11 active oil rigs in May, consistent with the number recorded in March.

Outlook and Implications

Oil prices are projected to remain elevated due to increased summer demand, heightened geopolitical risks in the Middle East, and expectations of an impending easing cycle by the Federal Reserve.

Money Market

During the review period, the banking system faced significant liquidity challenges as the opening position was predominantly negative. On average, banks' opening position was -₦187.91 billion, compared to - ₦180.21 billion in the previous quarter. This was primarily due to the Central Bank of Nigeria's aggressive monetary tightening. Consequently, the tight liquidity conditions in the banking sector led to a notable surge in short-term interbank interest rates. The average NIBOR rates (OPR/ON) rose sharply by 689 basis points to 28.76% in Q2 2024 from 21.87% in Q1 2024.
During this period, a total of N3.5 trillion was issued at the primary treasury bill market. Notably, the 91-day and 182-day treasury bill yields increased by 6 bps and 44 bps, respectively to 16.3% and 17.44%. However, the 364-day treasury bill yield decreased by 44 bps to 20.68%.

Outlook and Implications

The liquidity squeeze in the banking system is expected to persist as the CBN continues with its fight against inflation. Hence, we expect short-term interest rates to remain elevated. Additionally, fixed-income yields would remain high but could begin to decline gradually due to the rising debt service costs. Moody's, an international rating agency expects Nigeria's debt service cost to gulp 36% of government revenue in 2024.

Forex Market

The Naira appreciated to its highest level in six months at the start of the quarter, reaching ₦1,055/$, bolstered by the Central Bank of Nigeria's strong initiatives to rebuild confidence and improve transparency in the foreign exchange market. However, by the end of the quarter, renewed pressures emerged due to increased demand for forex outpacing its supply, causing the Naira to close the period at ₦1,515/$. Similarly, at the NAFEM window, the Naira initially strengthened to ₦1,072.74/$ early in the quarter but depreciated to ₦1,505/$ by the quarter's end.

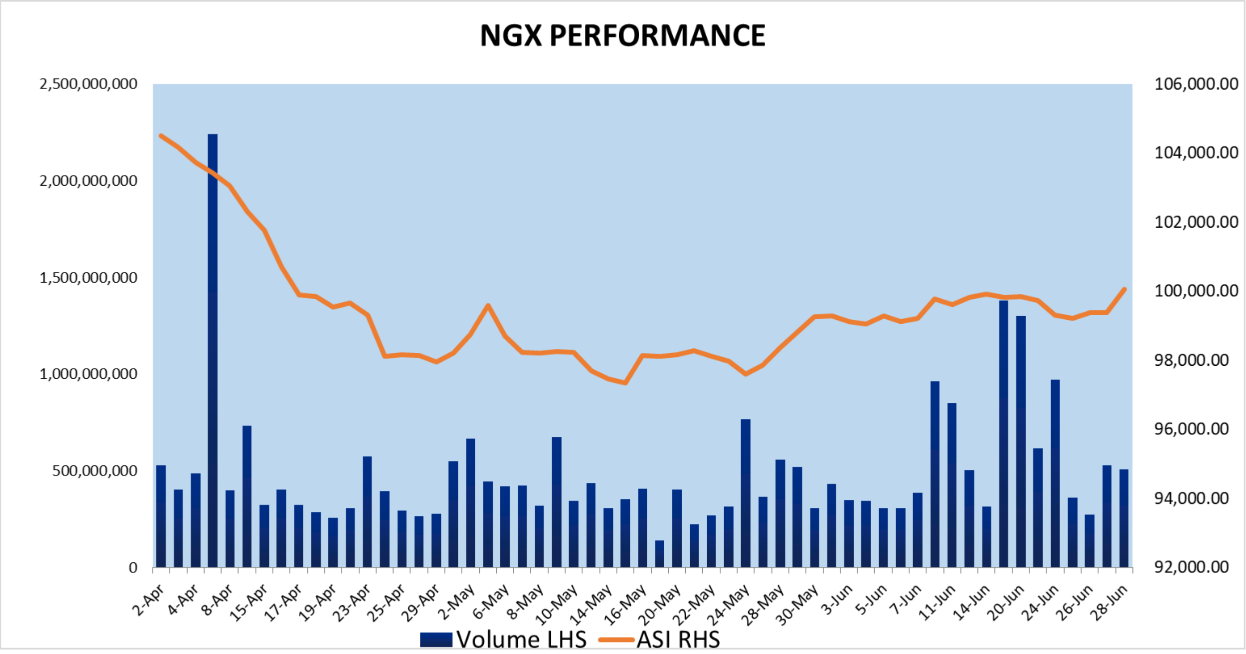
After a gradual decline at the start of the quarter, the gross external reserves rebounded and closed at $34.19 billion on June 28, up from $33.89 billion recorded on March 27.

Outlook and Implications

Dollar demand pressure would heighten in the near term due to the summer season. Unless there is a commensurate increase in the supply of dollars, the Naira is likely to face further depreciation in the short term. While the recent $2.25 billion World Bank loan will offer some support to the currency, it may not be sufficient to maintain a strengthening trend in the Naira.

Stock Market

The NGX All Share Index (ASI) ended the second quarter with a bearish tone, dropping by 4.31% to close at 100,057.49 points on June 28, down from 104,562.06 points on March 28. Similarly, market capitalization mirrored this trend, decreasing by 4.26% to ₦56.60 trillion on June 28 from ₦59.12 trillion on March 28. This decline in performance was mainly attributed to investors' preference shifting toward fixed-income securities, driven by their higher yields



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Research and Insights

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In Q2'24, the average trading volume declined by 12.09% to 499.54 million units from 568.24 million units in Q1'24, while the average trade value fell sharply by 24.59% to ₦9.26 billion from ₦12.28 billion in the previous quarter.

During this period, only the oil and gas sector posted gains, rising by 11.30%. Conversely, the banking sector saw a notable decrease of -19.37%, followed by the insurance sector (-3.79%), the industrial sector (-3.00%), and the consumer goods sector (-1.82%).

Market breadth was negative at 0.70x. Specifically, 47 stocks gained, 40 stocks remained unchanged, and 67 stocks recorded losses. Morison Industries Plc led the gainers with a substantial 152.84% increase in its share price. It was followed by Cutix Plc (69.23%), John Holt Plc (58.59%), Presco Plc (53.00%), and Cap Plc (50.00%). On the other hand, underperforming stocks included VFD Group Plc (-78.02%), PZ Cussons Nigeria Plc (-42.11%), First Bank Holding Plc (-38.40%), Nascon Plc (-34.35%), and Caverton Offshore Support Group Plc (-27.78%).

Outlook and Implications

We expect the market to experience volatility in the next quarter but with an overall positive trend. This outlook is based on the MPC's probable decision to maintain the status quo during its July meeting, which might boost investor confidence in the stock market.

Fixed Income Market

Two existing bonds were reopened in April (7-year maturing in FEB 2031 and 10-year maturing in FEB 2034), and two new bonds were issued in April and May (5-year maturing in APR 2029 and 9-year maturing in MAY 2033). The total amount offered in the bonds market decreased significantly to ₦1.35 trillion, marking a decline of 59.21% from ₦3.31 trillion in the previous quarter. Similarly, total allotment in Q2'24 also decreased by 45.61% to ₦1.30 trillion from ₦2.39 trillion in Q1'24. The marginal rates for the 5-year bond, 7-year bond, and 9-year bond were 19.64%, 20.19%, and 21.50% respectively.

Outlook and Implications

The MPC will meet later this month and expectations are that the committee will most likely leave all monetary parameters unchanged. Notwithstanding, we expect the yields on government securities to remain high.

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