Q1 2018 GDP Report: Its All About Oil to be Honest

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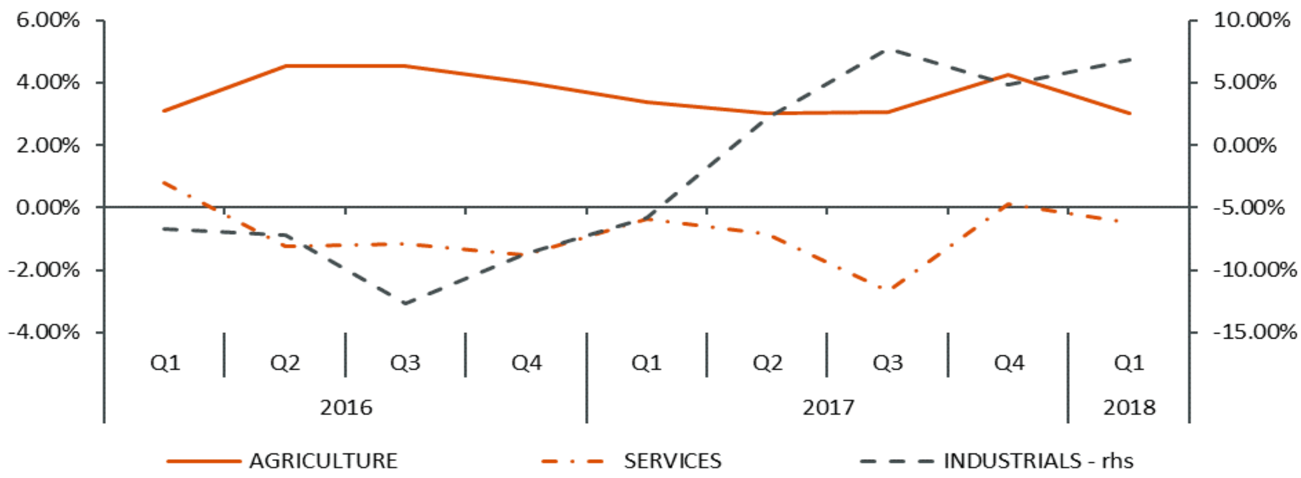
NIGERIA | MACRO | GDP

The National Bureau of Statistics released the Q1 2018 GDP report, which can simply be summarized as a case of the same song and dance. The overall GDP numbers printed at 1.95% y/y, with growth recorded in both the oil and non-oil sectors at 14.77% y/y and 0.76% y/y respectively (versus 11.20% y/y and 1.45% y/y respectively in Q4 2017). Even though the oil sector contributed only 9.61% to total GDP in Q1 2018 it remained the main driver of economic output. Growth in the oil sector can largely be attributed to the improved state of oil production in Q1 2018 with output averaging 2.0million barrels per day (mbpd) in Q1 2018, versus 1.75mbpd in Q1 2017.

Figure I: Major Sectorial Performances



Sources: NBS, Investment One Financial Services Research.

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Apathetic Non-Oil Sector Growth

The main cause of concern comes from the benign growth of the non-oil sector (Figure II below). Although the sector grew by 0.76% y/y in Q1 2018, it was however 70basis points (bps) lower than Q4 2017 readings. One of the main drivers of growth in the non-oil were Agriculture (3.00% y/y), which represented 22% of total GDP in Q1 2018, although the pace of growth slowed compared to Q4 2017 (4.23% y/y).

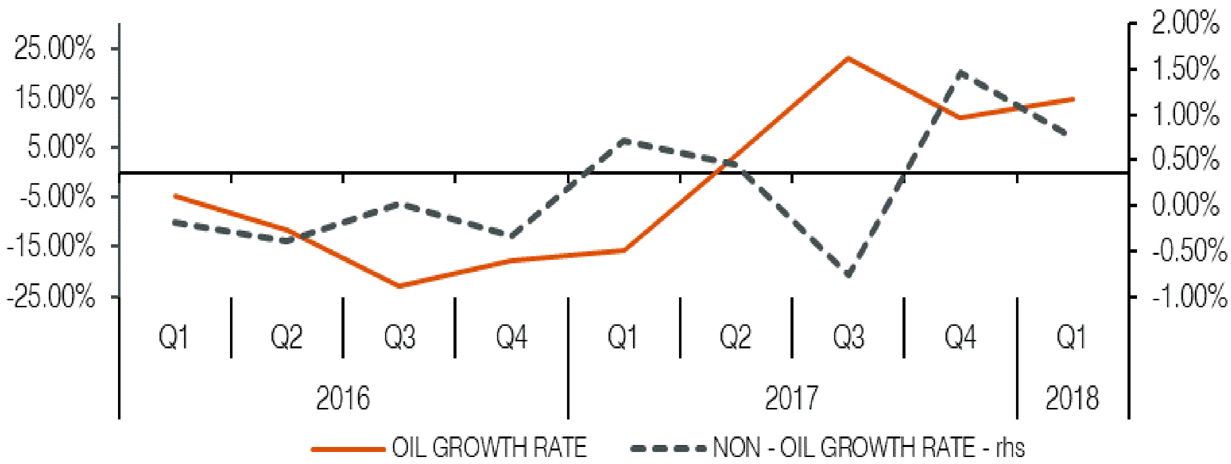
There was also support to economic activities from sharper growth levels recorded in Financial Institutions and Insurance (13.30% y/y) and Manufacturing (3.39% y/y) in Q1 2018. The slowdown in the Agricultural sector may not be unconnected with the tenacious conflict in the North. In real terms, the non-oil sector contribution to total GDP (90.39%) fell by 108bps y/y and 226 bps lower than Q4 2017.

On contrary, growth in the services sector, which contributed 55% to total GDP in Q1 2018, returned to negative territory still printed in the red as Trade (31% of services sector) and Real Estate (13% of Services sector) contracted by 2.57% y/y and 9.40% y/y respectively. Specifically, the Real Estate sector has now recorded a negative growth rate for the ninth consecutive quarter.

We highlight the divergence between the Manufacturing and Trade sectors and we view the positive momentum of the Manufacturing sector to be a reflection of an actual increase in inventories levels in the economy, in anticipation of higher demand as economic conditions continue to improve.

On the other hand, we view the trade sector performance as a reflection of the backlog of unpaid civil salaries, relatively high inflationary pressures (avg.14.27% in Q1 2018) on disposable income and consumer prices hindering consumer demand.

Figure II: Oil Sector vs. Non-Oil Sector

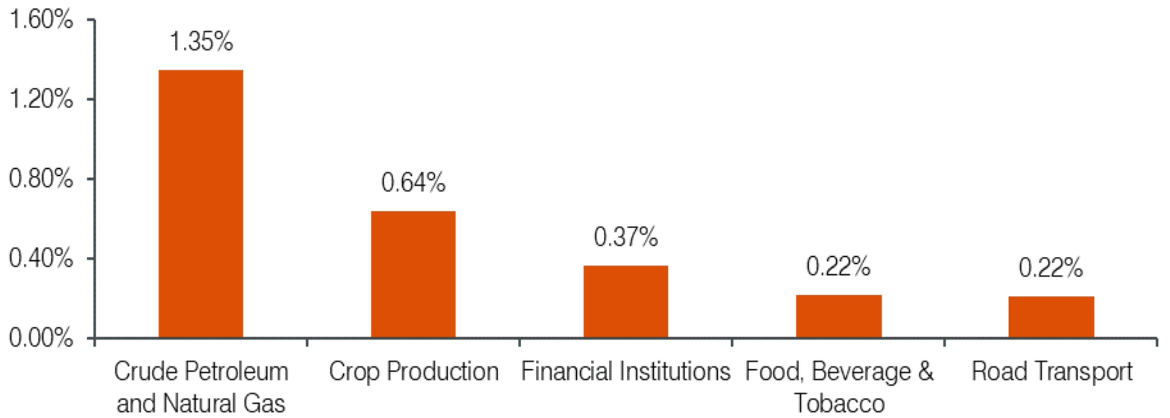


Sources: NBS, Investment One Financial Services Research.

Industrial Sector to the Rescue

Nonetheless, GDP output saw support from strengthening growth in the Industrial sector in Q1 2018 (24% of GDP and expanded by 6.86% y/y). Crude Petroleum and Natural Gas production was the largest contributor to growth (14.77% y/y) despite being less than 10% of total GDP in Q1 2018. Crop production came in second with 3.45% y/y, followed by Financial Institutions (12.58%) and Food, Beverage and Tobacco production (5.46%).

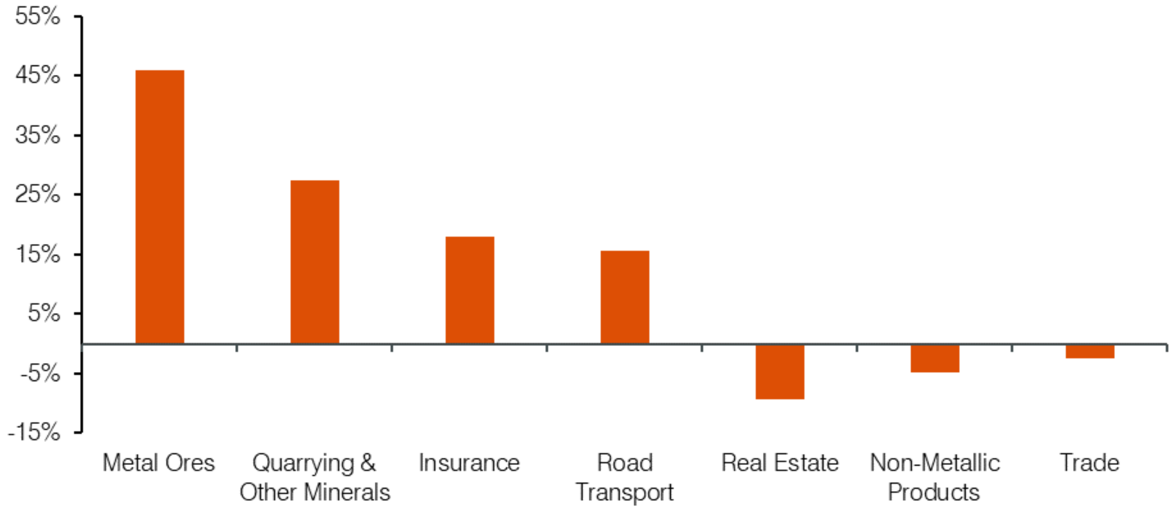
Figure III: Top Five Contributors to GDP Growth



Sources: NBS, Investment One Financial Services Research.

Oil refining grew on the back of the low base effect of Q1 2017 and maybe reflective of the NNPC's ongoing efforts in improving the utilization capacity of refineries. The growth in the cement sector may not be unconnected with the upswing in capex funding (NGN750billion) released into the economy towards the end of 2017. It is also reflective of the increase in volume performance Nigeria's biggest cement manufacturer, Dangote Cement, which reported a 5% y/y increase volume in Q1 2018. Almost all sub-sectors under the manufacturing sector witnessed significant expansion, which may not be unconnected with foreign exchange stability and improved liquidity and finally, the Central Bank of Nigeria's (CBN) tough stance on the banned 41 items from the official foreign exchange market. Furthermore, the CBN's Purchasing Manager Index also supported these numbers, as PMI readings (Q1 2018 - 56.77) remains well above 50 (which signals economic expansion). However, the construction sector printed negative and may well be attributable to the backlog of payments owed to contractors, estimated at N2.7trillion as well as the much delayed 2018 budget .

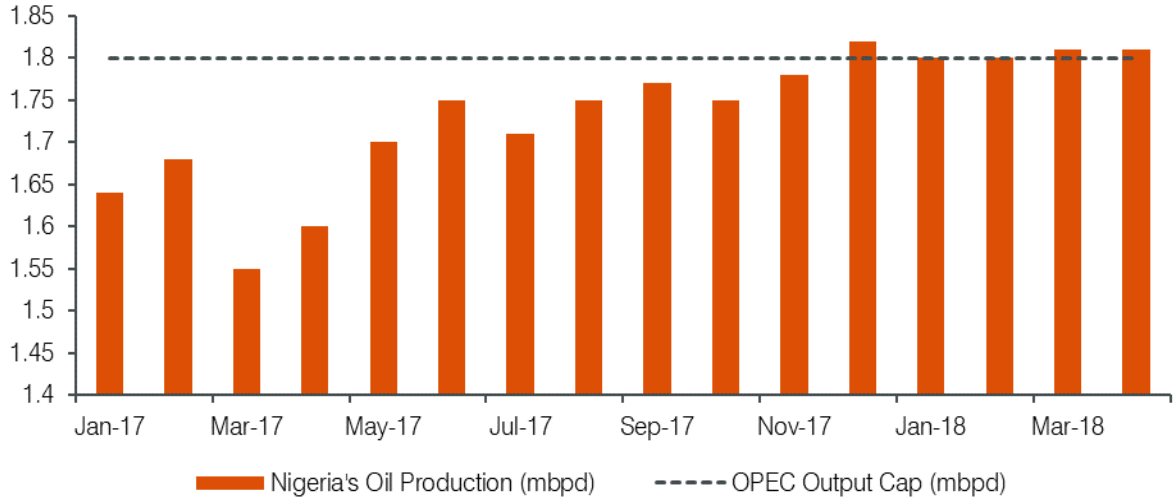
Figure IV: Best and Worst Performing Subsectors



Sources: NBS, Investment One Financial Services Research.

Going forward, we highlight the effect of the low base effect of Q1 2017 on the Q1 2018 growth numbers. The major driver of which was the upswing in crude oil production could wane off in H2 2018, as oil production had already picked up to 1.87mbpd which is very similar to the current rate of production levels at 2.0mbpd (including condensates) as at April 2018. This figure would further be impacted by what appears to be a temporary closure of the Trans-Forcados pipeline in May 2018 for repairs, which could take off 250,000 - 400,000bpd from production. We also highlight the potential effect that the OPEC's cap at 1.8mbpd (excluding condensates) may have on the production levels and growth in the sector, especially with Seplat's on drilling five new wells in 2018. Oil refining on the other hand remains a major issue in the country and the historically volatile performance could eventually weigh in on output in Manufacturing subsector and consequently, the Industrial sector.

Figure V: Nigeria's Crude Oil Production (excluding Condensates)



Sources: Bloomberg, Investment One Financial Services Research.

In conclusion, while these GDP numbers point to continuous expansion in economic activities, the oil sector's contribution remains the main driver of GDP. The torpid growth rate of non-oil sector remains a huge concern. Two lessons we learnt from the recession that plagued the economy from Q1 2016 – Q1 2017 were: I. The need to diversify economic drivers/government revenue and II. Bridging the infrastructural deficit. From the figures above, it appears we are still not where we should be yet and while the GDP numbers are positive, it is really uninspiring.

The Senate has once again passed the budget in May, leaving little time to improve on the rate of capex implementation (2017: 63.5%). There is a need for a more aggressive approach to economic reforms that would bridge the infrastructural deficit and even at that, the effect of these reforms may not be seen till 2019.

Furthermore, the continuous dependence on oil leaves the economy vulnerable to shocks that may arise if there is an uproar of violence in the Niger Delta. The real estate sector of the economy continues to plunge as the sector as a result of weak consumer sentiment and high cost of funding.

However, given the current low yield environment and the potential for a reduction in the Monetary Policy Rate, we think this might be a catalyst for growth in the Real Estate and Trade sectors as we anticipate increased credit lending to these sectors. The trade sector should also benefit from election spending and the potential upward review in the national minimum wage in H2 2018, as we believe this would boost consumer spending and activities in that sector.

Worthy of note however, is the ICT sector, which has been in a recession since Q2 2017. Both the Telecoms (up 1.88% y/y) and Publishing (up 12.53% y/y) subsectors helped boost sector output. The improvement in this sector should serve as a catalyst for the much anticipated MTN IPO in H2 2018.

Overall, we maintain our FY 2018 growth forecast of 2.5%

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