26 October 2018

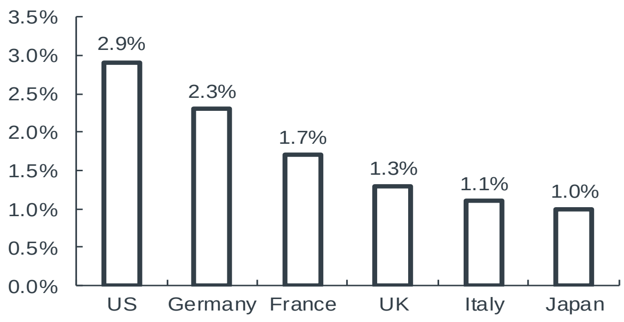
Weekly economic and market update.
Overview of markets in the week ended 26 October 2018

Global economy

Data released during the week showed the US economy expanded by an annualized 3.5% in the third quarter, beating polled market expectations of 3.3%. This comes lower than the 4.2% growth record in the previous quarter, which was the highest since Q3-14. The increase was a result of positive contributions from personal consumption expenditures (PCE), private inventory investment, state and local government spending, federal government spending, and non-residential fixed investment that were partly offset by negative contributions from exports and residential fixed investment. **The contraction in GDP growth largely reflects impact of the drag on net trade, caused by the trade wars led by the Trump administration.**

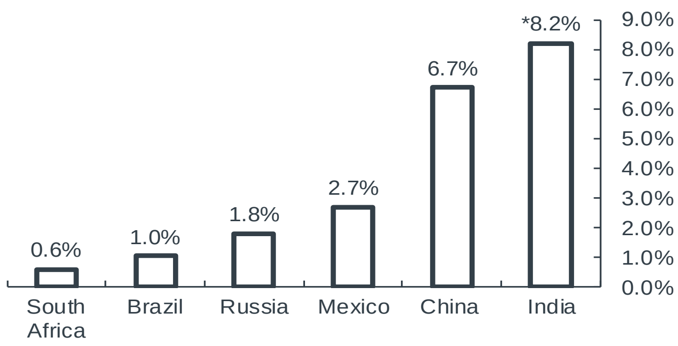
In line with market expectation, the European Central Bank (ECB) left policy rates unchanged and stressed that they will remain at present levels, at least through H1-2019. Precisely, interest rate, deposit rate and lending rate were left unchanged at 0.0%, 0.25% and -0.4% respectively. Barring any negative surprises from the incoming inflation data in the medium term, the ECB explains that it is on track to ending its quantitative easing program (EUR15 billion monthly) this year. **With the relatively stable pace of economic growth, the ECB has scaled back on its stimulus packages despite growth concerns in Italy and persisting trade protectionism**

Fig 1: Annualized GDP growth rate Q2-2018 – DMs



***Source**: Bloomberg, Cordros Research*

Fig 2: Annualized GDP growth rate Q2-2018 – EMs



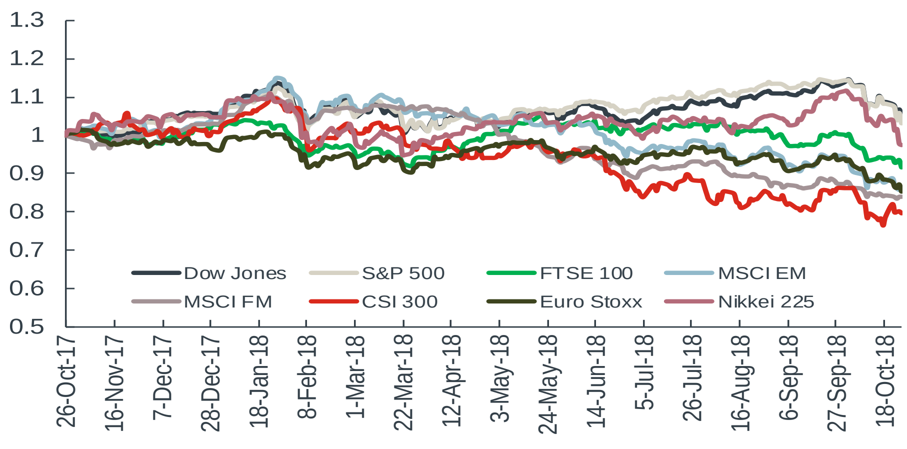
**Q1-2018*

***Source**: Bloomberg, Cordros Research*

Global markets

Losses resurfaced across most global markets within our coverage, save for China, which gained 1.23% during the week – halting two weeks of losses. On the other hand, investors in the US (S&P 500: -4.77%, DJIA: -3.59%), Euro area (FTSE 100: -2.66%, Euro Stoxx 50: -3.61%), and Japan (Nikkei 225: -5.98%) recorded significant losses, following geopolitical concerns and disappointing corporate earnings and economic data. The returns in emerging (MSCI EM: -2.32) and frontier (MSCI FM: -0.41%) markets also remained in negative territory, owing to losses posted in India (-2.82%) and Brazil (-0.56%), as well as in Kenya (-0.30%) and Morocco (-0.43%), respectively.

Fig 3: Global indices (index of 1)



***Source**: Bloomberg, Cordros Research*

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Nigeria

Economy

The Central Bank of Nigeria (CBN) released its Consumer Expectations Survey Report for Q3-2018. It shows that consumers' overall outlook improved in Q2-2018 with the index increasing to 1.5 points (vs. -6.3 points in Q2-2018 and -10.5 points in Q3-2017). Respondents attributed the change in outlook to improved economic conditions. The consumer outlook for the next quarter and next 12 months were also positive at 24.7 and 30.1 points respectively, attributable to the expected increase in net household income, the anticipated improvement in Nigeria's economic conditions, and expectations of increased savings over the next 12 months. **The improving consumer expectation suggests higher aggregate demand and positive performance for businesses.**

According to the Minister for Budget and Planning, the Federal Executive Council has approved the government's 2019-2021 Medium-Term Expenditure Framework and Fiscal Strategy Paper which proposes NGN8.73 trillion expenditure for the 2019 Budget. The government forecasts GDP growth of 3% next year, and assumes oil output of 2.3mb/d, crude oil price at USD60 per barrel, and an average exchange rate of NGN305/USD. **We note that the planned expenditure is down 5% from the NGN9.12tr planned in 2018, some recognition that the economy is under pressure, as the country struggles to meet revenue targets.**

Table 1: Macro indicators

Macro indicators (Nig)	Current	Year start	Forecast
Real GDP growth	1.50%	2.11%	1.83 (Q3-18)
MPR	14.00%	14.00%	14.00% (Next meeting)
CPI	11.28%	15.37%	11.33% (Oct-18)
Exchange rate (USD)	NGN306.55	NGN305.50	NGN306.60 (2nd Nov)
Foreign reserve (USD'bn)	42.34	38.91	41.97 (2nd Nov)
Unemployment	18.80%	18.80%	20.30% (Q4-17)
Brent crude oil price (USD)	77.41	66.57	82.00 (2nd Nov)

***Source**: CBN, Bloomberg, NBS, Cordros Research estimates*

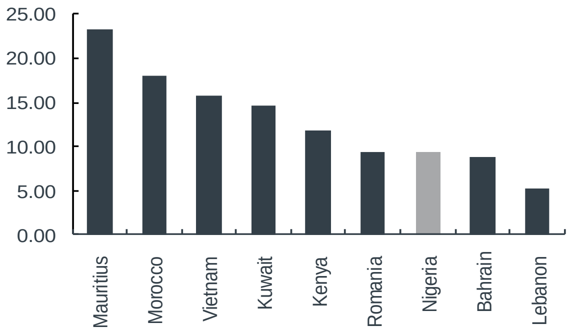
Capital markets

Equities

The equities market closed the week positive for the third consecutive week, amidst a week of mixed corporate earnings releases. The benchmark index inched up 0.20% to 32,907.33 points, with all sessions of the week posting gains, save for a DANGCEM-led loss of 2.37% posted mid-week. Month-to-Date return remained in positive territory, at 0.43%, while the Year-to-Date loss moderated to 13.95%. The Oil & Gas index led other major sectoral indices in gains, followed by the Banking and Insurance indices, while the Consumer Goods and Industrial Goods indices posted losses. Market breadth was negative, with 39 losers and 26 gainers, led by WAPCO and DIAMONDBNK, respectively.

Despite recent gains, we remain conservative in our outlook for equities in the short to medium term, amidst brewing political concerns, and the absence of a positive trigger. However, stable macroeconomic fundamentals remain supportive of recovery in the long term.

Fig 4: Trailing 12M P/E ratios (frontier market)



***Source**: Bloomberg, Cordros Research*

Table 2: Top gainers and losers

Gainers				Losers			
Ticker	CP * (NGN)	WTD	YTD	Ticker	CP * (NGN)	WTD	YTD
DIAMONDBNK	1.44	20.00%	-4.00%	WAPCO	18.25	-13.10%	-59.35%
LAWUNION	0.58	16.00%	-24.68%	BETAGLAS	62.10	-11.54%	21.03%
FIDELITYBK	2.09	10.58%	-15.04%	AGLEVENT	0.36	-10.00%	-48.57%
ROYALEX	0.22	10.00%	-56.00%	UPDCREIT	8.10	-10.00%	-19.00%
JBERGER	23.70	9.98%	-15.36%	PORTPAINT	2.52	-10.00%	14.55%

****CP: Closing price***

***Source:** NSE, Cordros Research*

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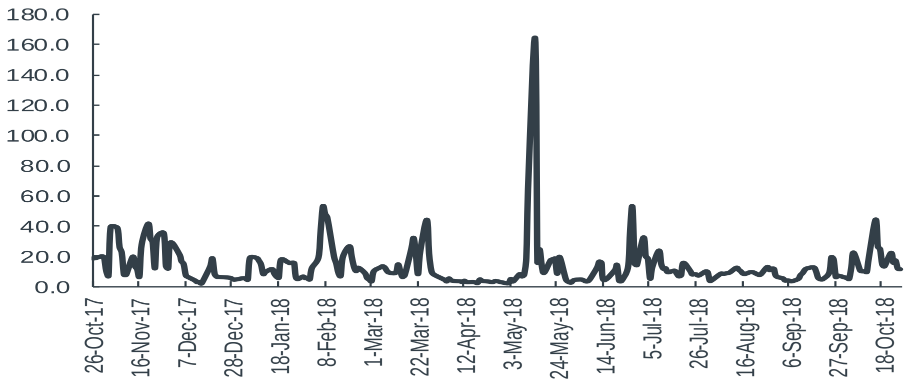
Fixed income and money market

Money market

The overnight lending rate shed 192 bps, w/w, to 11.42%, against last week's close of 13.33%. Rate was elevated through to mid-week following outflows from wholesale FX sales. However, inflows from (1) matured OMO bills (NGN372.88 billion) and retail FX refunds (c. NGN200 billion) on Thursday boosted liquidity. The CBN conducted the usual OMO auction, selling a total of NGN186.02 billion worth of bills.

Next week, inflows totaling NGN770.42 billion -- maturing OMO bills (NGN381.88 billion), FAAC disbursements to states and local governments (NGN382.52 billion), and bond coupon payments (NGN6.02 billion) -- are likely to outweigh outflows; thus, boosting system liquidity. In effect, a contraction in the overnight lending rate is on the cards.

Fig 5: Overnight money market rate (%)



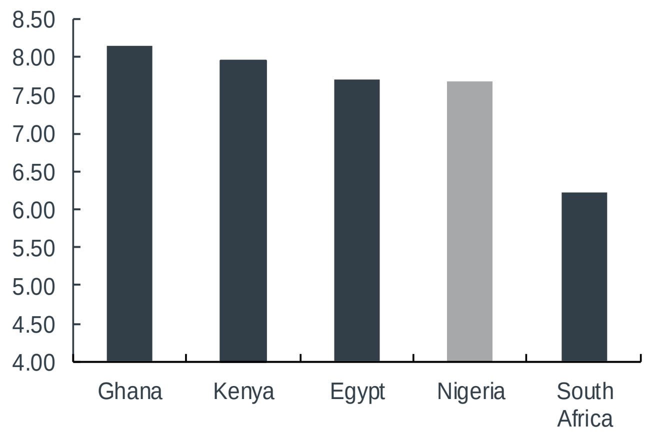
***Source**: FMDQ, Cordros Research*

Treasury bills

Activities in the treasury bills market were bearish as market players sold off on the back of (1) tightened liquidity position, and (2) hikes, for the second consecutive week, in the rates of all the bills – 98DTM, 182DTM, 364DTM – on offer at the OMO auction to 11.50% (+25 bps from 11.25% previously), 13.00% (+25 bps from 12.75% previously), 14.50% (+50 bps from 14.00% previously), respectively. As a result, yields rose 20 bps on average, w/w, to close at 13.73%. Sell pressure was spread across the mid (+21 bps) and long (+62 bps), with the 111DTM (+96 bps) and 328DTM (+77 bps) bills recording significant yield expansions, respectively. Conversely, demand for the 34DTM (-87 bps) bill led to yield contraction at the short (-5 bps) end of the curve.

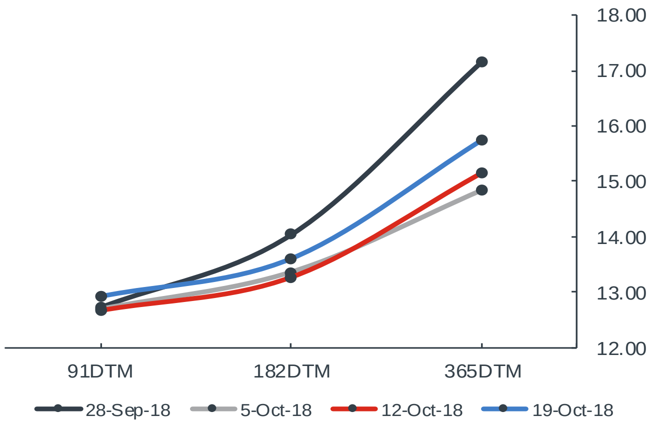
Yields are expected to fall in the coming week, supported by expected buoyant system liquidity. At the NTB auction scheduled for next week, the CBN will offer NGN145.29 billion – NGN9.54 billion of the 91-day, NGN47.71 billion of the 182-day, and NGN88.04 billion of the 364-day – worth of bills to the market.

Fig 6: Yield on 10-year eurobonds (Nigeria vs. African peers) (%)



***Source**: Bloomberg, Cordros Research*

Fig 7: T-Bills yield curve (%)



***Source**: FMDQ, Cordros Research*

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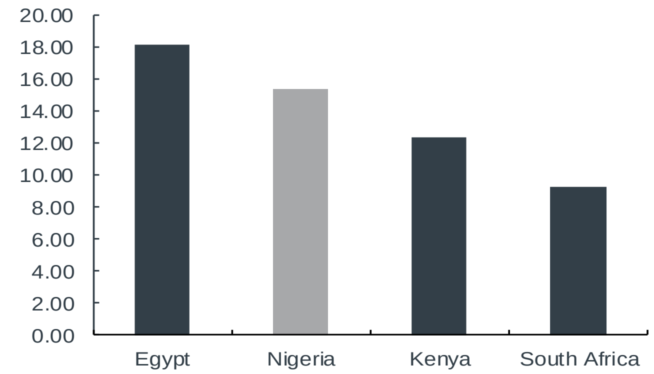
Bond

The bond market opened the week on a bearish note, as market players sold off ahead of the primary auction. The increase in short term rates (as discussed above) further widen rates, leading to a 7bps w/w expansion in average yield to 15.06%. Yields expanded across the short (+13 bps) and mid (+9 bps) segments, following selloffs of the FEB-2020 (+36 bps) and JAN-2026 (+22 bps) bonds, respectively. On the flip side, there was demand at the long (-3 bps) end of the curve, with yield on the JUL-2034 (-10 bps) bond recording the largest contraction. At this week's primary auction, the DMO allotted a total of NGN88.08 billion – NGN12.65 billion of the APR-2023 (re-opening), NGN20.14 billion of the MAR-2025 (re-opening), and NGN55.29 billion of the FEB-2028 (re-opening) – in bonds (vs. NGN115 billion offered), at respective stop rates of 15.00% (same as previous auction), 15.15% (same as previous auction), and 15.32% (vs. 15.2459% at the previous auction).

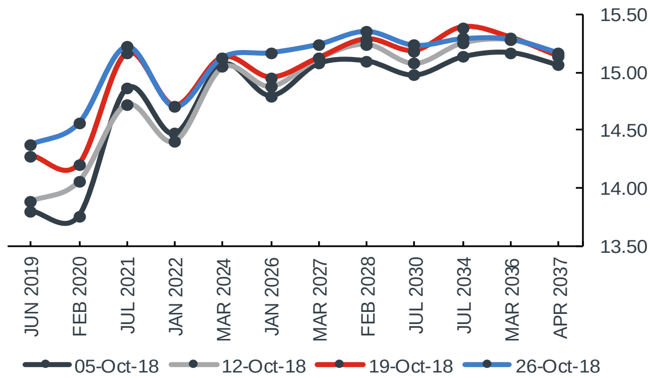
Our theme for the bond market favours modestly higher yields in the medium term, anchored on (1) domestic monetary policy direction, (2) sustained uptick in inflation rate, (3) capital flight amid higher yields in safe haven assets, and (4) political uncertainty stemming from the upcoming general elections.

Fig 8: Yield on 10-year LCY bonds (Nigeria vs. African peers) (%)



***Source**: Bloomberg, Cordros Research*

Fig 9: FGN bond yield curve (%)



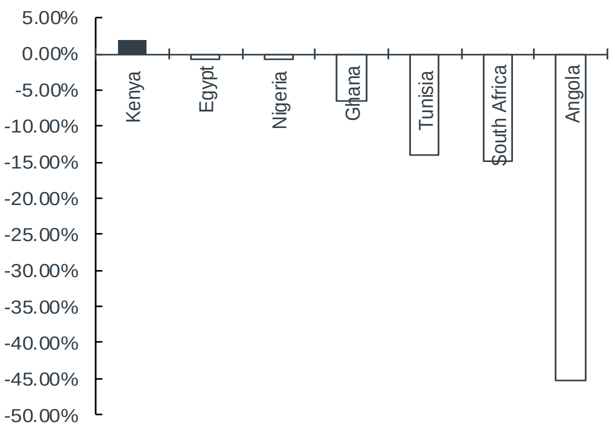
***Source**: FMDQ, Cordros Research*

Foreign exchange

The USD/NGN remained flat at NGN362 in the parallel market, while it appreciated by 0.05% to NGN363.84 in the I&E FX window. Total turnover in the IEW rose by 36.4% to USD1.114 billion, against USD816.78 million recorded last week. Meanwhile, the foreign reserves continued to deplete during the week, dropping USD375.67 million to USD42.34 billion. In the FX forwards market, the USD/NGN strengthened across most of the major dated contracts – 1-month (+0.07%), 3-month (+0.04%) and 6-month (+0.07%) dated contracts to NGN367.26, NGN374.08 and NGN384.99 respectively -- while it depreciated by 0.47% in the 1-year contract to NGN409.92.

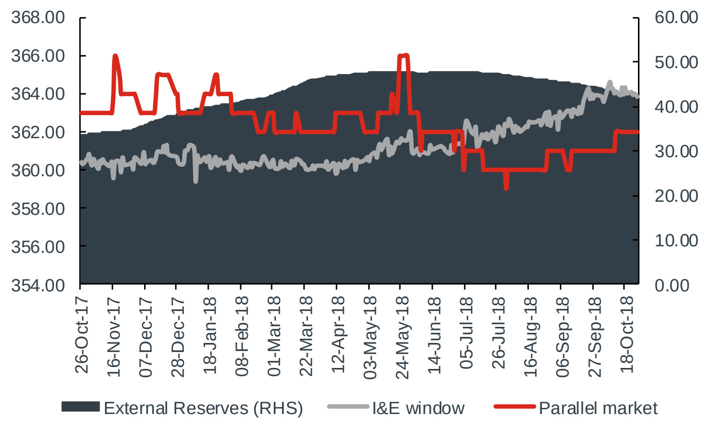
The naira is expected to continue trading within current bands, as the still-healthy level of the reserves – despite recent depletion -- supports the apex bank's interventions in the forex market.

Fig 10: USD/NGN vs other African currencies (YtD returns)



***Source**: Bloomberg, FMDQ, CBN, Cordros Research*

Fig 11: USD/NGN exchange rate vs. external reserves (USD'bn)



***Source**: Bloomberg, FMDQ, CBN, aboki FX, Cordros Research*

Top business headlines of the week

- FG, states, LGs record N43bn shortfall in allocation
- New population control policy coming, says Fed Govt
- FG to float N100bn Sukuk in December
- NNPC: Nigeria’s gas reserves now 202trn cubic feet
- CBN raises capital requirements for microfinance banks
- Nigerians spend $8b annually on importation of vehicles – Osinbajo

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