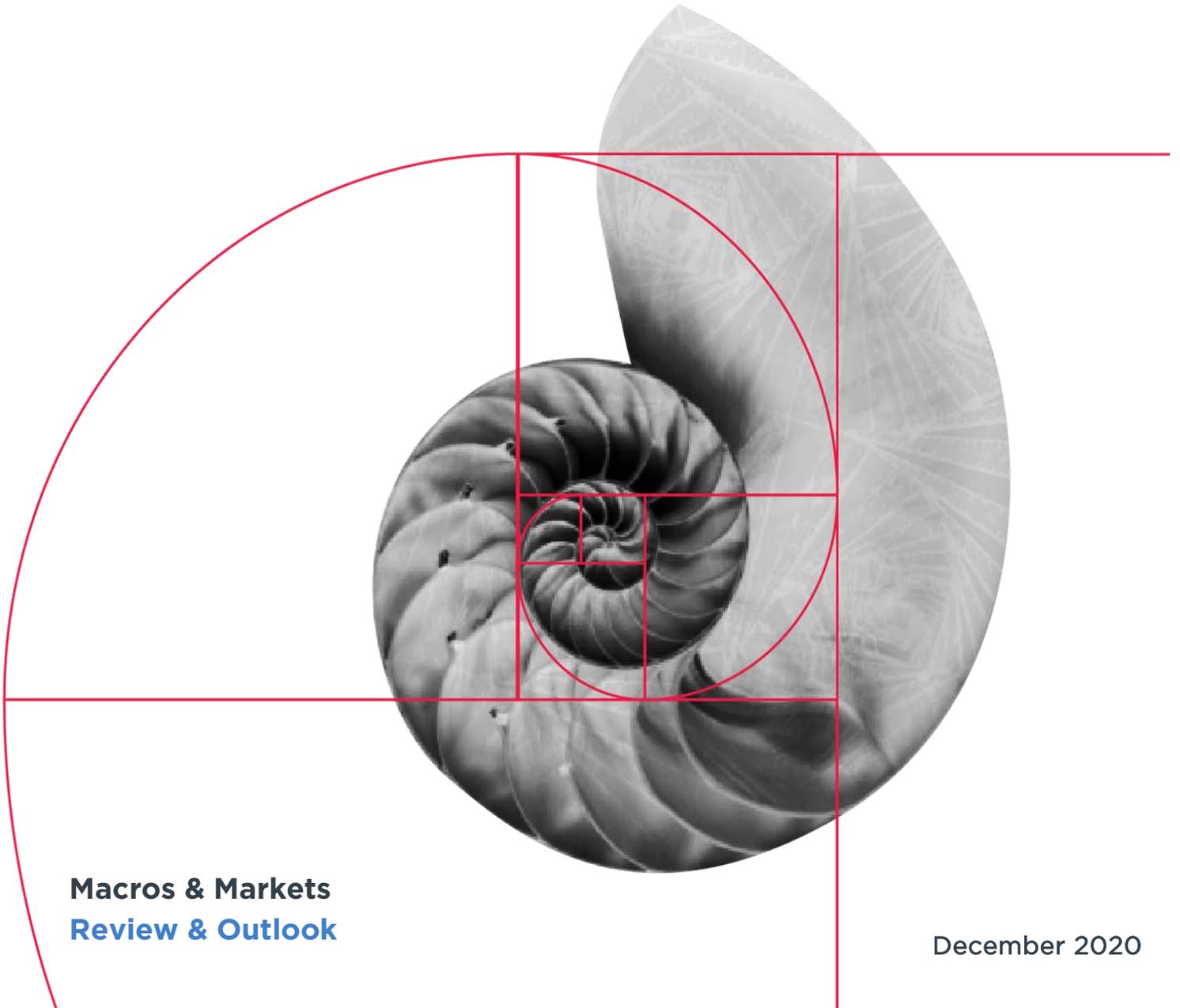


Nigeria

in 2021. *Positioning in the New Normal.*



Executive Summary.

The Credit crisis of 1772; the Great Depression of 1929–39; the 1973 Oil crisis; the Asian Financial crisis of 1997; the Global Financial crisis of 2007–08. None has originated from a biological factor. 2020 brought a completely different twist. The year featured unprecedented shutdowns of economic activity due to a pandemic that overwhelmed the health care systems of many advanced economies. A fusion of massive monetary and fiscal stimulus packages, the historic OPEC+ oil production cuts, and a vote for new leadership in the US also characterised the year. As 2020 draws to a close, it is shaping up to be among the worst years for the global economy in more than 70 years.

In our [2020 Mid-Year outlook](#), we aligned with the view that without a vaccine, it was unlikely that economic activities would pick up pace anytime soon. Looking ahead now, we do see some silver linings. Breakthroughs on Covid-19 vaccines are being announced each week, and following encouraging early efficacy data, the hope is that most economies can return to a new normal following a widespread rollout of the vaccine in Q2-2021. Though challenges remain, we think the global recovery is sustainable, synchronous and supported by policy. The preceding, in our view, should culminate in the V-shaped recovery, which began in May, being sustained, and leading to 5.2% global GDP growth in 2021, according to IMF estimates.

On crude oil, our views on a rebound on global demand, as stated in our 2020 Mid-Year Outlook, played out in H2, with the resurgence of COVID-19 in Europe and the US leading to a slightly larger decline in global demand for the year. We expect the recovery in demand to continue, supported by the expansion in global growth. However, we still maintain the view that demand will likely not return to pre-COVID-19 levels before the end of 2021, especially as we expect a protracted vaccine rollout. On a balance of factors, we forecast Brent crude price will average between USD45.00 and USD50.00/bbl in 2021. This forecast is a slight increase from a projected USD42.00/bbl for 2020E but still significantly lower than the 2019 level of USD64.16/bbl.

The ravaging impact of the twin shocks (the pandemic and downturn in oil prices) may have dissipated following the re-opening of economies. Still, the cog in the wheels of economic activities will linger in 2021. Although we expect the economy to recover from the deep contraction in 2020, we believe policymakers will be faced with the more difficult task of lifting output growth above population growth. Consequently, the recovery will remain mostly insufficient in

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boosting per capita income, stimulating employment opportunities, and addressing the growing disparity in income levels.

We are cautiously optimistic that the land borders, which were re-opened on 15th December, will ease pressures in food basket given weak domestic capacity. Nonetheless, we expect the gradual increase in electricity tariffs and higher distribution costs linked to higher PMS prices (especially if oil prices gain momentum) to offset the gains.

Despite the FX management strategies put in place by the CBN to reduce FX demand for importation, we expect the current account to be pressured by a faster increase in imports compared to exports. The pressure will be amplified by a wider deficit in the services account, based on our expectations on improvement in the scale of international airline operations and medical-related tourism. Taking into consideration the fragility of macroeconomic conditions coupled with the lingering liquidity constraints in the I & E window, we expect FPI inflows to remain tepid. This view, alongside our expectation of a marginal increase in export earnings, implies accretion to the FX reserves will be limited, thus, hindering the ability of the CBN to defend the local currency.

On monetary policy, we believe the MPC will be at a crossroads. They will be faced with the difficult choice of keeping interest rates low to support economic recovery while easing government financing pressures or tightening to attract FPIs to mitigate currency pressures and restore stability in the external sector. We expect the MPR to remain unchanged in Q1-21 but envisage tightening from Q2 onwards, due to our expectations on inflation and the need to stem currency pressures.

On fiscal policy, we expect budget performance to be characterised by the recurring themes of underperformance in revenue targets, sub-optimal CAPEX spending relative to recurrent expenditure, and weak revenue from State-Owned Enterprises (SOEs). Ultimately, we believe the government will be faced with the difficult task of balancing borrowings to support economic recovery and avoiding a further buildup of debt that will further weaken debt sustainability metrics.

This has been a truly exceptional year in, and outside of financial markets. The performance of the fixed income market outstripped that of all traditional asset classes, as a combination of market dynamics and policy actions resulted in yields paring to record low levels. Also, Nigerian equities sank to 8-year lows as investors ran to safety due to the pandemic but also saw a rapid recovery to 2-year highs as the hunt for yield intensified.

We believe that the performance in the fixed income market will be a tale of two halves. We expect yields to remain in the low single-digit territory through H1-21, with a moderate uptrend to account for reduced market participation as investors seek yields in other asset classes. However, in the latter part of the year, we believe that a combination of (1) weak market participation, (2) revision of monetary policy to a tightening cycle, (3) widening fiscal deficit, and (4) fragile macroeconomic environment will lead to an increase in yields over 2021.

Similar to the fixed income market, we also expect it to be a tale of two halves for Nigerian equities in 2021, with the market delivering further upside in the first half of 2021 before retracing slightly in the second half on an expected reversal in fixed income yields. The sources of risks remain plenty, the macro story remains uninspiring, and valuations are elevated. However, we think the mix of (1) elevated liquidity, (2) low interest rates, (3) attractive dividend yields, and (4) earnings recovery argues in favour of an extension of the equity bull market into 2021.

We present our views on the different sectors we cover in the following sections:

We are 'Overweight' on **Nigerian Banks**, as we expect a combination of (1) strong dividend yield expectations, and (2) resiliency of sector players into the FY-21 financial period to support price performances. Our picks are ACCESS (BUY; TP: NGN13.80), FBNH (BUY; TP: NGN8.50), GUARANTY (BUY; TP: NGN41.07), UBA (BUY; TP: NGN11.24), and ZENITHBNK (BUY; TP: NGN32.28).

In **Nigeria's Cement Sector**, volume growth in 2021e will be modest due to the lingering impact of the pandemic on government finances and household income. Although the stiff competitive landscape coupled with soft industry conditions will deter industry players from raising prices substantially, we still see scope for marginal increases in prices. We expect **Dangote Cement (BUY, TP: NGN252.68)** to deliver decent EPS growth of 2.9% in 2021E. For **Lafarge Africa, (BUY, TP: NGN29.53)** we believe the company's focus on the Nigerian market and continued gains from the deleveraging of its balance sheet, following the sale of the loss-making South African operation, will remain supportive of earnings. We estimate the company will deliver EPS growth of 3.7% in 2021E.

For Consumer Staples, it's a mixed bag. **Agriculture** stocks are likely to benefit from improved volumes from new maturities. However, the border reopening is a significant risk to pricing and by extension top-line growth. **Brewery** stocks are expected to record better volume growth in 2021FY, mostly due to the low base from 2020FY. However, the ability of brewers to increase prices above inflation remains constrained. Surging inflation and FX illiquidity will also put pressure on input costs and margins. We expect similar for **Food & HPC** stocks. However, we like the agro-allied names in salt [**NASCON (BUY; TP: NGN20.49)**] and sugar

[**DANGSUGAR (BUY; TP: NGN26.63)**] due to each business' capability to fully price in movements in international prices and currency depreciation into the pricing of their products.

In Telecoms, there is a potential negative impact on Q1-21 revenues and earnings if the NCC does not extend the NIN registration deadline and lines are disconnected. However, we like that **MTNN (BUY; TP: NGN202.21)** is putting necessary measures in places to mitigate the disruptions. Consequently, we are conservative on subscriber growth in 2021E (+7.7% vs. 13.3% in 2020E). The start of the company's PSB operations remains the key catalyst for the stock as mobile money in Nigeria presents a compelling growth/return opportunity for MTNN, in our view. However, over the medium to long term, the growth of Nigeria's and MTNNs subscribers will continue to be underpinned by its attractive demographics as well as the structural upsides.

For Oil & Gas (Downstream), we forecast the price of PMS to average between NGN165.00/litre and NGN175.00/litre in 2021. Our view is hinged on our higher average oil price assumption (USD45.00 - USD50.00/bbl) in 2021. We expect demand for white products to return to pre-pandemic levels as the economy reopens. On supply, with current structural issues still existent, we expect the NNPC to remain the sole avenue for product sourcing. **Our top pick for the sector is TOTAL (BUY, TP: NGN147.94).**

Equity Views by Sector

		Overweight 	Neutral 	Underweight 
SECTOR	POSITIVES	NEGATIVES	INDUSTRY	VIEW
Communications Services VIEW 	<ul style="list-style-type: none"> – Low penetration provides a significant upside for revenue – PSB license approval is a key catalyst 	<ul style="list-style-type: none"> – Heightened regulatory risk – Promotions could intensify and affect pricing 	Telecoms	
	<ul style="list-style-type: none"> – Improved cost-efficiency – New maturities to boost volumes 	<ul style="list-style-type: none"> – Risk to CPO pricing from illegal importation following border reopening 	Agricultural Producers	
Consumer Staples VIEW 	<ul style="list-style-type: none"> – Slightly higher pricing – Premiumisation to cushion margin pressure 	<ul style="list-style-type: none"> – Consumer wallet remains pressured – Competition still intense – On-trade demand channels hit by restrictions 	Brewery	
	<ul style="list-style-type: none"> – Valuations are undemanding – Substantial price increases expected from agro-allied producers 	<ul style="list-style-type: none"> – Consumer wallet remains pressured – Competition still intense 	Food and Household & Personal Products	
Financials VIEW 	<ul style="list-style-type: none"> – Valuations remain compelling – Attractive dividend yields 	<ul style="list-style-type: none"> – Low yield environment will hurt margins – Increased regulatory risk poses systemic risk 	Banks	
Industrial Goods VIEW 	<ul style="list-style-type: none"> – Government CAPEX to boost cement demand – Marginal prices increase 	<ul style="list-style-type: none"> – Sustained border closure a risk to exports 	Cement	
Oil & Gas VIEW 	<ul style="list-style-type: none"> – Increased demand as economy reopens – Higher PMS prices and margins 	<ul style="list-style-type: none"> – FX illiquidity to impede imports – Inflation to put pressure on distribution costs 	Downstream (Refining & Marketing)	

Source: Cordros Research

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Global.

Growth.

The Darkness Before the Dawn

- We think the global recovery is sustainable, synchronous and supported by policy.
- Global growth in 2021 to print 5.2% y/y (2020E: -4.4% y/y).

The Credit crisis of 1772; the Great Depression of 1929–39; the 1973 Oil crisis; the Asian Financial crisis of 1997; the Global Financial crisis of 2007–08. None has originated from a biological factor. 2020 brought a completely different twist. The year featured unprecedented shutdowns of economic activity due to a pandemic that overwhelmed the health care systems of many advanced economies. A fusion of massive monetary and fiscal stimulus packages, the historic OPEC+ oil production cuts, and a vote for new leadership in the US also characterised the year. As 2020 draws to a close, it is shaping up to be among the worst years for the global economy in more than 70 years. In our view, China will be the only large economy to record any growth this year, and according to IMF estimates, the US economy will have shrunk by 4.3%, with advanced economies as a whole and emerging markets contracting by 5.8% and 3.3% respectively. **Overall, we expect global GDP growth to fall to 4.4% in 2020.**

In our 2020 [Mid-Year outlook](#), we aligned with the view that without a vaccine, it was unlikely that economic activities would pick up pace anytime soon. Looking ahead now, we do see some silver linings. Breakthroughs on Covid-19 vaccines are being announced each week, and following encouraging early efficacy data, the hope is that most economies can return to a new normal following a widespread rollout of the vaccine in Q2-2021. Though challenges remain, we think the global recovery is sustainable, synchronous and supported by policy. **The preceding, in our view, should culminate in the V-shaped recovery, which began in May, being sustained, and leading to 5.2% global GDP growth in 2021, according to IMF estimates.**

Figure 1: Historical Global growth (%)

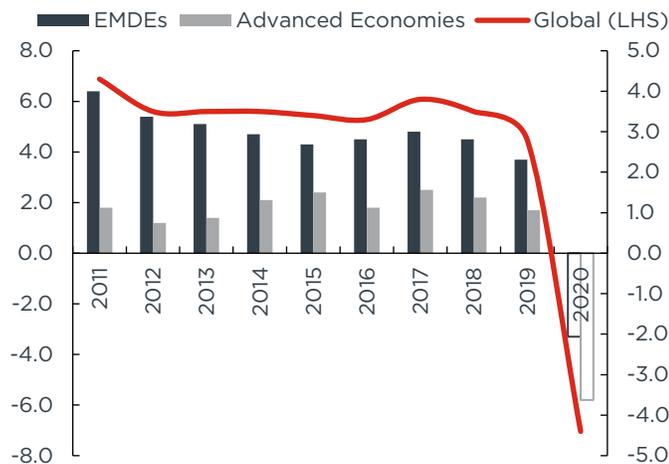
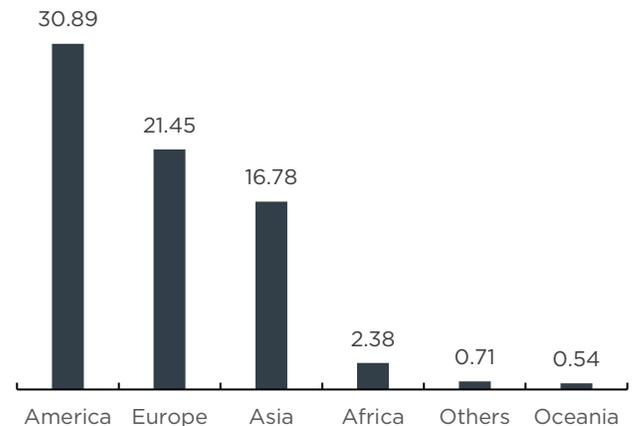


Figure 2: COVID-19 cases (million) per continent (as at Dec. 15th)



Source: IMF, ECDC, Cordros Research

The Pandemic Leaves a Scar on Global Growth

At the start of the year, we expressed that global growth would be precarious on the back of the Sino-US trade tensions, which manifested at the tail end of 2019. The outbreak of the COVID-19 pandemic however tilted global growth to a more profound decline as different countries imposed strict lockdown measures to limit the impact of the worldwide health crisis, which later deteriorated into a worldwide economic crisis. The pandemic disrupted global trade and supply chains while emerging markets experienced capital outflows amid declines in commodity prices. For one, countries decided to protect their citizens by limiting the movement of goods to other countries. For context, India, Thailand, and Vietnam placed restrictions on exports of critical food items such as rice and eggs. Between March and May, there was an unprecedented outflow of c. USD100.00 billion in debt and equity funds from emerging markets, resulting in precipitous declines in the prices of risk assets, while heightened concerns regarding the possibility of increased defaults led to an increase in the cost of both sovereign and corporate debt.

In limiting the impact of the global pandemic on households and corporates organisations, policymakers implemented massive fiscal and monetary stimulus packages, more than the level seen since the Great Depression. On the one hand, monetary authorities adopted accommodative monetary policies and quantitative easing programs. The fiscal authorities, on the other hand, rolled out sizeable fiscal stimulus packages to boost aggregate demand and support cash flow for firms. The unprecedented size of stimulus packages (c. USD22 trillion or c. 20% of the global economy) coupled with the re-opening of economies in May

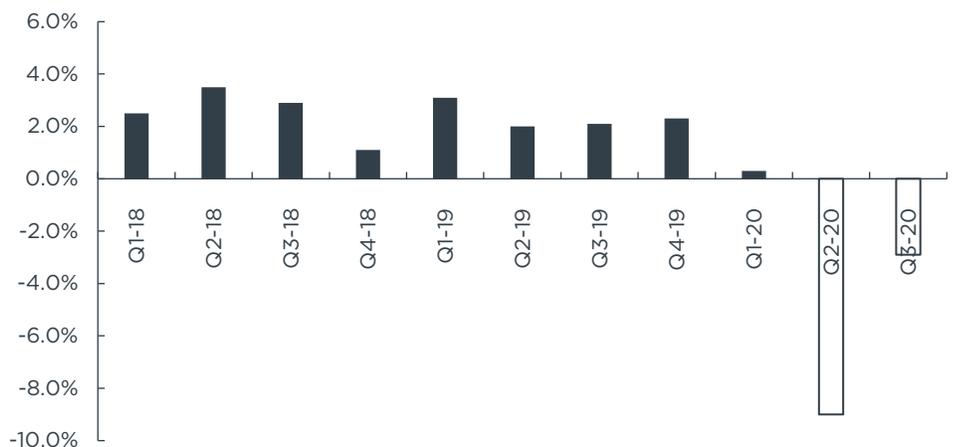
and June rescued the global economy from the depths to which it had plunged in April.

Accordingly, the IMF, in its October 2020 World Economic Outlook, revised the global growth estimate for 2020 to -4.4% y/y from -4.9% in June 2020. The revised estimate was, however, still worse than during the 2008/2009 global financial crisis when global GDP shrunk by 1.8% and materially weaker when compared to 2019: +2.8% y/y. However, a critical downside risk to this projection is the renewed lockdown measures embarked upon by countries to tackle the second wave of the pandemic.

Developed Economies the Worst Hit

The United States witnessed a record decline in economic activities in the first half of the year, as pandemic-induced lockdown measures derailed economic activities. US GDP contracted by 9.1% y/y in Q2-20 (Q1-20: -5.0% y/y) on a seasonally adjusted basis, confirming a technical recession. A blend of a 34.6% y/y decline in private consumption (c.60.0% of GDP), as well as a significant downturn in business investment (-27.0% y/y on a seasonally adjusted basis), primarily drove the contraction. In Q3-20, private consumption (+40.7%) rebounded following government stimulus package (c. USD3 trillion) which supported unemployed persons and businesses. As a result, the US economy grew by 7.4% y/y in Q3-20. Similarly, business equipment investment (+70.1%) and residential investment (+59.3%) also rose significantly as the low-interest environment boosted housing and credit growth.

Figure 3: Trend in US GDP growth

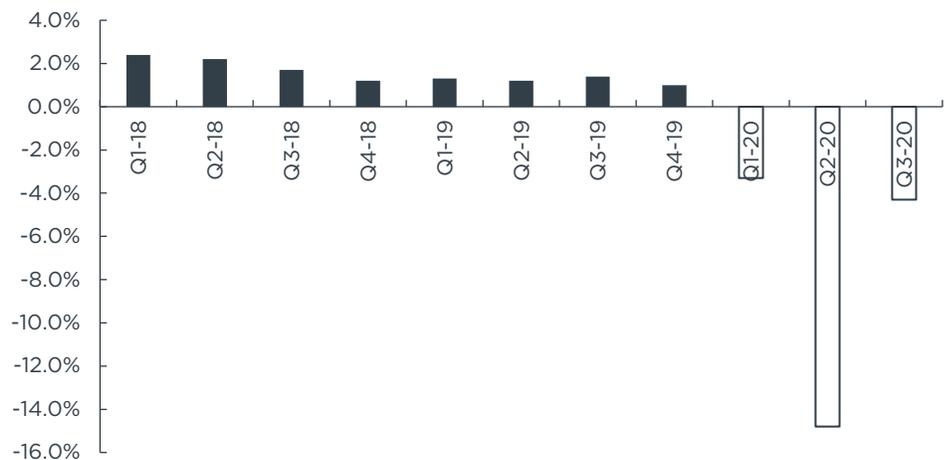


Source: Bureau of Economic Analysis, Cordros Research

Economic performance was also devastating in the Euro Area, especially in Italy, Spain, France, and Germany, which became the hotspots of the pandemic

in the region. Notably, Italy implemented a compulsory lockdown on 10th March, which halted economic activities in the state, especially the service sector, the most significant component of the economy. Disagreements between frugal states (Austria, Denmark, Sweden, and the Netherlands) and the other members on the proportion of grants to repayable loans delayed support in the form of fiscal stimulus. The Euro Area shrank by 15.0% y/y in Q2-20 compared to a negative growth rate of 3.1% y/y in Q1-20. Although the Euro Area rebounded by 12.7% quarter-on-quarter on a seasonally adjusted basis, preliminary estimates by Eurostat shows that growth in the region declined by 4.3% in Q3-20 when compared to the corresponding period of 2019. Further out, 'Brexit' uncertainties continue to dampen manufacturing and industrial activities, thus adding to the economic woes created by the global health crisis.

Figure 4: Trend in the Euro Area GDP growth (%)

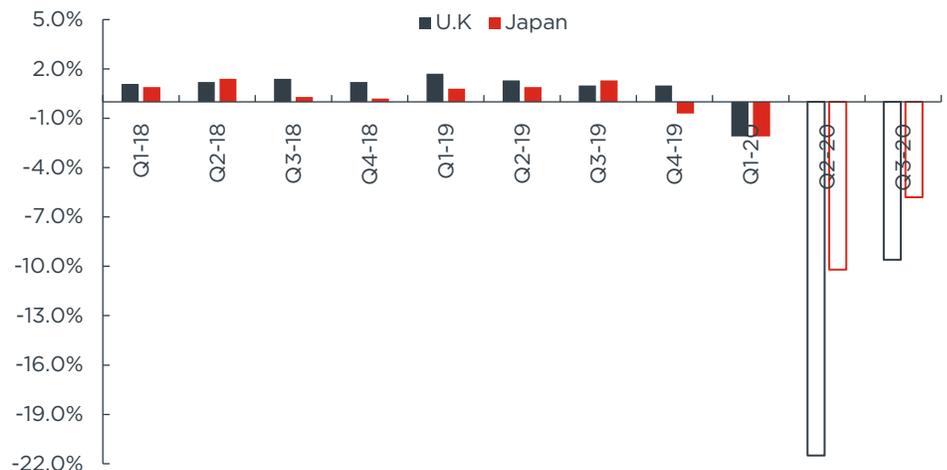


Source: Eurostat, Cordros Research

The United Kingdom's economy entered a technical recession in Q2, as GDP contracted by 21.5% y/y in Q2-20 (Q1-20: -2.1% y/y) – the largest contraction on record since the Office of National Statistics (ONS) began keeping records in 1955. The contraction translated to the UK economy being 22.1% smaller than it was at the end of 2019. The outturn in the second quarter reflected the impact of lockdown measures in March through May to contain the spread of the virus. Production activities declined due to company closures, weak domestic and external demand as well as labour shortages (following job losses and staff furloughs). Demand for other contact-dependent services also stalled. In response to the growing number of COVID-19 infections, the UK government in the last week of Q3-20 announced further restrictions for the immediate six months period or until it saw evidence of a noticeable slowdown in new infection rates.

In Japan, economic contraction in Q2-20 was the largest since at least 1955 as the state of emergency and lockdowns in the country's major export markets hampered consumer spending, production, and exports. Accordingly, GDP shrank by 10.2% y/y in Q2-20 (Q1-20: -2.1% y/y). Private consumption, which accounts for 56.0% of GDP, fell by 8.2% (Q1-20: -0.8%). The decline was due to a significant fall in spending on retail and travel due to the lockdown. Exports also dropped by 18.5% (Q1-20: -5.4%) as overseas demand for Japanese goods fell against the backdrop of weak global demand. In August, the country's Prime Minister, Shinzo Abe, announced his decision to step down due to health reasons. He was most popular for his belligerent stance on defence and foreign policy. He left a legacy of political stability as well as a strong centralised power base that allowed forceful stimulus policies to revive the economy. The stimulus packages ranged from monetary easing to government spending and economic reforms that lead to measurable growth during his first term but waned after that, thus raising questions about the long-term sustainability of some of his policies. In Q3-20, the Japanese economy rebounded sharply by 21.4% q/q on a seasonally adjusted basis on the back of (1) 20.1% q/q growth in household spending following the ease of movement restriction, (2) Growth in public spending by 9.3% q/q, and (3) record growth in exports (31.3% q/q). On a year-on-year basis, economic output in Japan contracted slowly by 5.8% in Q3-20.

Figure 5: GDP growth (%) in Japan and the UK.



Source: Eurostat, Cordros Research

The Emerging Economies Also Bow to the Pandemic

Except for China (Q2-20 GDP: +3.2% y/y) and Vietnam (+0.39% y/y) which recorded positive GDP growth, many emerging and frontier market economies experienced significant negative growth in the second quarter of 2020, with a few currently in recession. For instance, Brazil (Q2-20: -10.9% y/y vs. Q1-20: -

0.3% y/y) and Mexico (Q2-20: -18.7% y/y vs. Q1-20: -1.4% y/y), experienced two consecutive quarters of negative growth. The confluence of the reduced trade volumes linked to weakness in external demand, subdued private consumption, and business investment dragged economic activity in the region.

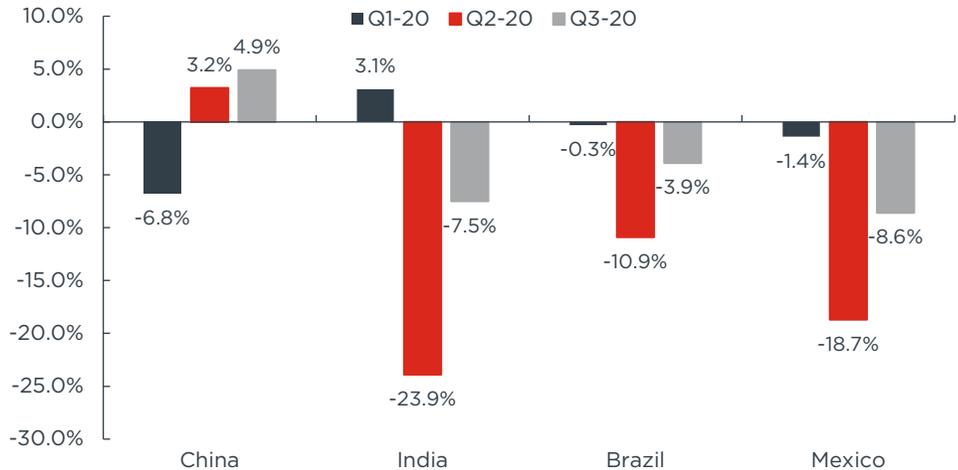
To put this into context, economic activities in China declined in Q1-20 as the country embarked on lockdown measures to curtail the spread of the COVID-19 pandemic. The actions, in conjunction with the already weak external demand emanating from the trade war with the US, dragged Q1-20 growth to -6.8% y/y - the first decline since at least 1992. The contraction in growth led the government to embark on a massive fiscal stimulus program to the tune of CNY3.6 trillion (USD506 billion) to mitigate the adverse impacts of the pandemic. By April, the country embarked on a gradual normalisation of activities while trade also improved due to the robust external demand for pharmaceutical and electrical products. Hence, China recorded a positive growth of 3.2% y/y in Q2-20. By August, export activities had improved rapidly, following improvement in global demand as countries gradually lifted the COVID-19 containment measures. Following the momentum in Q2-20, the Chinese economy grew further by 4.9% y/y in Q3-20 although below the consensus estimate of 5.2% y/y. The services sector (+4.3% y/y), and retail sales (+0.9% y/y) drove the expansion, signalling the recovery was driven by consumption compared to the state-backed industrial recovery in Q2-20.

Away to India, growth moderated in Q1-20 as the first seven days of the country's nationwide lockdown coincided with the last seven days of Q1-20, leading to the weakest growth since the global financial crisis. Specifically, GDP slowed to 3.1% from 4.1% y/y in Q4-19., with the services sector being the worst hit. In Q2-20, the full impact of the pandemic on India's economy was more pronounced as GDP slumped by 23.9% y/y - the lowest level on record reflective of the feedback effect arising from the closure of business activities.

Similarly, Brazil, which was already battling with subdued growth before the pandemic had to impose social distancing measures that constrained economic activities. As such, growth declined by 0.3% y/y in Q1-20 (vs. Q4-19: +1.6% y/y). The contraction was largely driven by moderation in private consumption (-2.0% y/y) and retail sales (-1.1% y/y) in the final month of the quarter. Government expenditure also slowed down (+0.2% y/y vs Q4-19: +0.4% y/y) following the continued tightening of public finances. In Q2-20, the growth rate drifted further into the negative territory (-10.9% y/y on a seasonally adjusted basis), as the COVID-19 pandemic made economic agents cut down on household and capital spending. By Q3-20, the decline in economic output softened to 3.9%

y/y in line with the easing of the COVID-19 containment measures as well as the impact of the fiscal stimulus in firming up activities.

Figure 6: GDP growth (%) in emerging and developing economies



Source: NBS, CSO, Trading Economics, Cordros Research

In Africa, lower commodity prices and weak external demand related to the slowdown in the global economy, amid pre-existing structural constraints, stalled growth in the continent. The weakness was evident in tourism and commodity-dependent economies which contracted due to the impact of the global pandemic on commodity prices and the services sector.

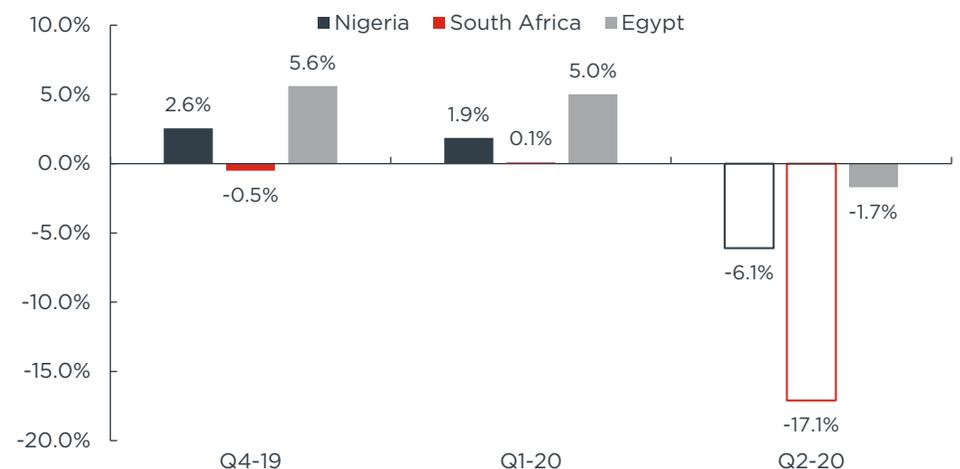
For context, we saw weak performance in Nigeria (Q2-20: -6.10% y/y), the continent's heavyweight, due to the decline in both the oil (Q2-20: -6.63% y/y) and non-oil (Q2-20: -6.05%) sectors. While the oil sector declined due to partial compliance with the OPEC oil cut agreement, restrictions put in place to mitigate the spread of the COVID-19 pandemic dampened activities in the non-oil sector. Similar trend ensued in Q3-20 as the full compliance with OPEC+ agreement and compensation for the overproduction in Q2-20 dragged the oil sector growth by 13.89% y/y. In comparison, the non-oil sector declined by 2.51% y/y as the COVID-19 pandemic continued to have a lingering impact on business activities amid the lifting of restrictions. Sequentially, the Nigerian economy declined by 3.62% y/y in Q3-20 – thus falling into economic recession.

Growth plummeted to the worst on record in South Africa, reflecting the impact of the COVID-19 lockdown measures on domestic activities. With the pandemic, business sentiment weakened, consumers held off on non-essential spending while mining activities slowed down amid weak external demand. Specifically, growth in Q2-20 declined significantly by 17.1% y/y (Q1-20: +0.1% y/y) as household consumption expenditure (-49.8% y/y vs. Q1-20: +0.2% y/y),

fixed investment (-59.9% y/y vs. Q1-20: -18.6% y/y) and external sector (-7.4% y/y vs. Q1-20: +3.9% y/y) all plummeted on a seasonally adjusted annualized rate (SAAR). Just like Nigeria, the only exception among the activity sectors was the agricultural sector which grew, albeit slower, by 15.1% y/y (vs Q1-20: 26.8% y/y) on high production of field crops as well as horticultural products.

Elsewhere, Egypt's GDP slowed to 3.5% in 2020FY (July 2019 - June 2020) compared to +5.6% y/y in the first half of the fiscal year, due to the decline in the activities in the tourism sector, as well as the decline in gas prices in the international market.

Figure 7: GDP growth (%) in the African economies



Source: NBS, Stats SA, NSO, Cordros Research

Synchronized Dovish Stance across Major Central Banks

Since the onset of the pandemic, global monetary authorities set out to be in sync in terms of monetary policy as they not only reduced their key interest rates but also increased money supply through quantitative easing programs.

The Federal Open Market Committee (FOMC) of the US Federal Reserve cut its benchmark interest rate twice in March (50bps to 1.25% on 3rd March and 100bps to 0.25% on 15th March). Also, it launched a quantitative easing program worth USD700 billion (USD500 billion worth of treasuries and USD200 billion of mortgage-backed securities). Since then, the FOMC has elected to keep the federal funds rate near zero (0%-0.25%).

In Europe, the European Central Bank (ECB) expanded its existing asset purchase program by EUR120.00 billion in a bid to support bank lending, and at the same time launched a EUR750.00 billion Pandemic Emergency Purchase Program (PEPP) in March. It increased this by EUR600 billion to EUR1.35 trillion in June.

Meanwhile, the rate on the main refinancing operations, marginal lending facility, and deposit facility remain unchanged at 0.0%, 0.25%, and 0.50% respectively.

In Asia, the Peoples' Bank of China (PBOC) cut interest rates cumulatively by 30bps to 3.85%- 10bps rate cut in February to 4.05% – the first cut since October 2019 and another 20bps cut on 20th April. Additionally, the five-year Loan Prime Rate (LPR), which is a key reference rate for mortgage lending, was also lowered by 10bps to 4.65%. Since then, the bank has left the benchmark interest rates unchanged.

Table 1: Macroeconomic Indicators across Selected Countries

	US	Euro Area	UK	Japan	China	India
YTD rate decision	-150bps	Unchanged	-65bps	Unchanged	-30bps	-115bps
Latest Inflation Rate	1.2%	-0.3%	0.7%	-0.4%	0.5%	7.6%
Unemployment Rate	6.7%	8.4%	4.8%	3.1%	5.3%	7.0%
Equity Market (YTD return)	4.8%	-6.1%	-13.7%	15.3%	11.7%	9.1%

Source: IMF, Trading Economics, Cordros Research

Fiscal Authorities also Rolled Out Stimulus Packages

Beyond existing automatic stabilisers, fiscal authorities also responded through increased government spending and expansion of safety nets to protect the vulnerable segments of the population.

In Europe, a pan-European crisis stimulus fund totalling EUR1.28 billion (an increase of EUR750 billion in July from EUR540 billion in May) aimed at funding the development of treatments and vaccines, providing liquidity support to companies, and protecting workers and jobs affected by the pandemic is in place.

Elsewhere, the US launched a stimulus package of an estimated USD2.30 trillion under the CARES act, which was aimed at but not limited to; (1) providing one-time tax rebates to individuals, (2) expanding unemployment benefits, (3) providing food safety nets for the most vulnerable, (4) preventing corporate bankruptcy, and (5) helping small businesses to retain workers. With economic data suggesting that the impact of the stimulus packages is gradually waning out, there have been ongoing discussions in the US Congress to pass a more robust fiscal stimulus which will cater to the needs of the people and strengthen the recovery process.

China announced a total fiscal package of CNY4.60 trillion (c. 5% of GDP) in May – the most extensive economic rescue plan in its history – aimed at (1) boosting business investment, (2) improving the healthcare system, and (3) improving the

general welfare of the people through accelerated disbursement of unemployment insurance, tax relief and waived social security contributions.

How Quickly Will The World Recover?

Over 2021, we expect growth to vary among countries, with commodities export and tourism-dependent countries expected to face weaker recovery compared to countries that are reliant on the industrial sector. Besides that, the global growth momentum is also subject to trade, and investment positions among nations as the uncertainty that comes with the pandemic could make countries limit their interactions with the external sector to protect their citizens. However, sustained monetary policies, varying degrees of fiscal stimulus, and people's adaptation to voluntary social distancing are expected to cushion the negative impact, thereby partially bringing back economies from the peak of the crisis.

Thus, we expect global growth, to rebound, printing 5.2% y/y in 2021 (2020: -4.4% y/y). While the lingering impact of the stringent lockdown measures and the unrelenting trade war is expected to drag cumulative growth in advanced economies at 3.9% y/y (2020: -5.8% y/y), we believe a more robust performance in emerging markets and developing economies (+6.0% y/y) should neuter the impact, and by extension, bolster overall global growth outturn.

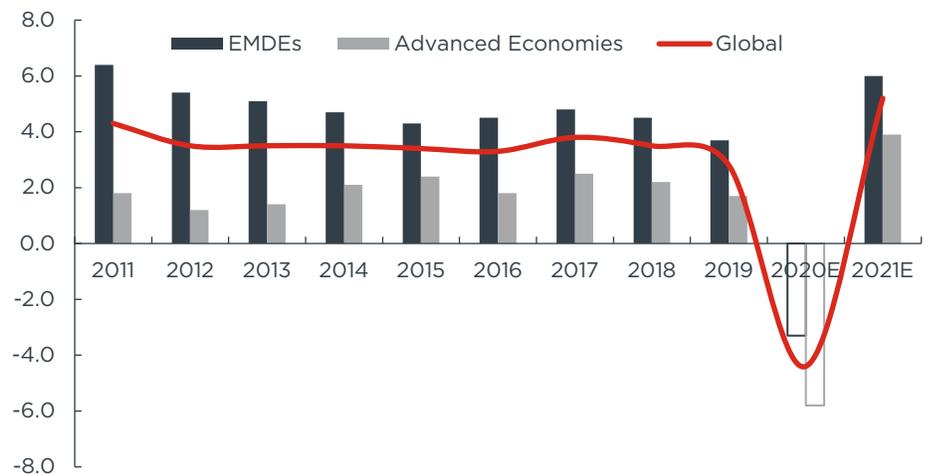
Across the developed economies, we expect growth to strengthen to 3.9% y/y in 2021 on account of robust fiscal and monetary stimulus to hasten the process of recovery. For the world's largest economy, the United States, we believe the encouraging news on the development of COVID-19 vaccines as well as the prospect of Food and Drug Administration (FDA) authorising the use of the vaccines before the end of 2020 should dissipate social distancing measures. The preceding should provide a tailwind for consumer spending and business sentiments over 2021 and will be further supported by sustained accommodative monetary policy and a possible USD908.00 billion economic relief package being debated upon by the US congress. Accordingly, we expect a rebound in domestic consumption and private investment. We note that prospects of de-escalation of trade tensions with trading partners on the back of a more friendly trade policy by the elected President could accelerate the pace of rebound in economic activities. Overall, we expect the US economy to grow by 3.1% y/y in 2021, a cyclical rebound from the projected decline of 4.3% in 2020.

Elsewhere, even as the blend of (1) the weaknesses in industrial output, (2) sluggish manufacturing activities, and (3) deteriorating domestic demand poses a threat to growth in the Euro area, we expect the low base, accommodative

monetary policy and fiscal stimulus packages to strengthen the recovery of the region by 5.2% y/y, recovering from the projected decline of 8.3% in 2020.

Although growth prospects continue to remain precarious and uncertain for many of the emerging markets due to the dependency on (1) commodity exports, (2) tourism, and (3) remittances, we expect economic output to grow by 6.0% on account of strong growth prospects in China which has resilient exports and strong policy support. Excluding China, the growth for emerging markets is projected at 5.0% for 2021, which will still leave output below pre-pandemic levels.

Figure 8: Trend in global growth and projection (%)



Source: IMF, Cordros Research

Risks: Renewed Lockdowns Ignite Doubt on Rebound in Global Growth

The continued spread of the pandemic, especially in advanced countries, threatens the recovery that started since the relaxation on stiff restrictions on economic activities. This development has fuelled concerns on the path of recovery in 2021. In our view, the most significant risk to a rebound in global growth over 2021 remains prolonged adoption of lockdown measures given its knock-on impact on activities in the manufacturing and services sector. Besides that, (1) uncertainty over the UK’s future trading relationship with the EU ahead of the Brexit transition terminal date of 31st December, (2) the low success rate in the search for effective and safe vaccines, (3) the possible withdrawal of fiscal countermeasures due to rising sovereign debt and weak debt affordability metrics by developing economies, and (4) the deterioration in global financial market conditions which would trigger a halt in lending to countries with inadequate fiscal buffers are significant downsides risks to global growth.

On a balance of factors, we believe the impact of the second round of lockdown will not be broad-based, and will also be less severe when compared to the global lockdown of Q2-20. Our prognosis is also hinged on not all countries across the globe embarking on renewed lockdowns as in Q2-20. As such, we expect the impact of these lockdowns on the global economy to be much smaller. Thus, leading to a slowdown to the recovery process in Q4-20, but for global growth to mostly be range-bound over 2021.

Crude Oil.

The Worst is Over, but the Recovery is Fragile

- Oil prices recovered slightly from the COVID-19 shock
- Demand will not return to pre-pandemic levels before the end of 2021
- Short-term risks are tilted to the downside.
- 2021E Brent crude price forecast: USD45.00 – USD50.00/barrel.

After plunging in March and April due to the shock of the COVID-19 outbreak, oil prices recovered robustly in May and June. The price of global benchmark, Brent crude, rose 154.8% (as of 4th December 2020) from its trough and was 29.1% higher on average in Q3-2020 (q/q). However, oil price remains c.23% below pre-pandemic levels. The recovery in prices was driven by (1) a sharp reduction in production, especially by OPEC+, (2) a modest recovery in consumption as lockdown measures were eased and travel and transport began to pick up, and (3) optimism around a vaccine rollout.

Figure 9: Crude Oil Prices in 2020 (USD per barrel)

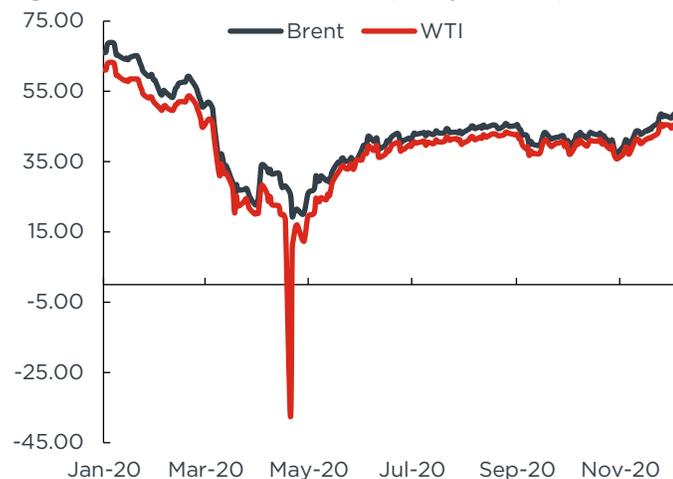
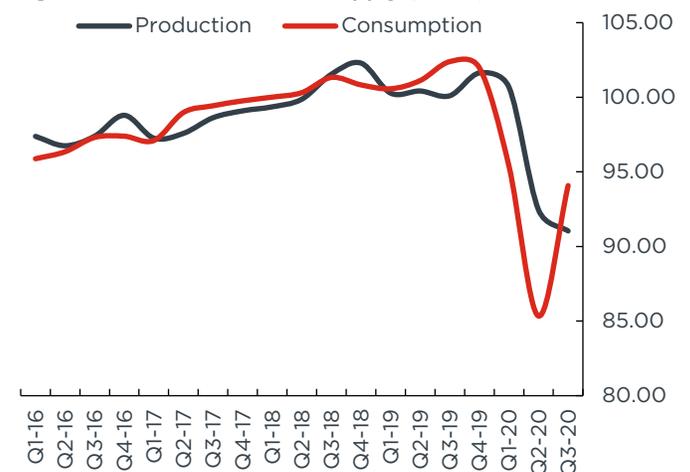


Figure 10: Global Demand & Supply (mb/d)



Source: Bloomberg, EIA, Cordros Research

Our views on a rebound on global demand, as stated in our [2020 Mid-Year Outlook](#), played out in H2, with the resurgence of COVID-19 in Europe and the US leading to a slightly larger decline in global demand for the year. We expect the recovery in demand to continue, supported by the expansion in global growth. However, we still maintain the view that demand will likely not return to pre-COVID-19 levels before the end of 2021, especially as we expect a protracted vaccine rollout.

On supply, the December 2020 OPEC+ meeting (which resulted in an agreement to easing the production cuts by lower than initially planned from January) sent

an important message that the OPEC+ will continue to cooperate and the group maintains the ability to move markets. While we expect non-OPEC output to rise in 2021, production in the United States is forecast to decline further, as low levels of investment in new production are insufficient to offset the rapid decline in output from existing fields. Despite a gradual tapering in production cuts, OPEC+ countries collectively have a significant amount of spare production capacity that is being held off the market. This excess capacity will keep a ceiling on oil prices.

Considering the preceding, we forecast Brent crude price will average between USD45.00 and USD50.00/bbl in 2021. This forecast is a slight increase from a projected USD42.00/bbl for 2020E but still significantly lower than the 2019 level of USD64.16/bbl.

Balancing the Market Will Be No Mean Feat

Demand: Due to COVID-19 lockdown measures and reduced mobility, oil demand is estimated to have fallen by 9.8 mb/d (-9.6% y/y) in 9M-20. Early estimates show a contraction of 5.2 mb/d (-5.1%) y/y in Q4-20, which will put the total demand contraction for 2020 at 8.6 mb/d (-8.5% y/y). These disruptions to transport and travel had a disproportionately large impact on oil consumption since transport fuels account for about two-thirds of global oil consumption. The fall in demand was broad-based but varied across countries, with substantial declines in the US and European Union (EU) (fig x). China, which was ground-zero for the pandemic, has seen the fastest recovery amid rebounding activity and stockpiling, with consumption in Q4-20 expected to be higher than the previous year. Elsewhere, oil consumption has started to recover as lockdown measures are lifted. As economic activities resume, we expect the recovery to continue, albeit gradually.

Figure 11: Petroleum demand by geography, y/y change (mb/d)

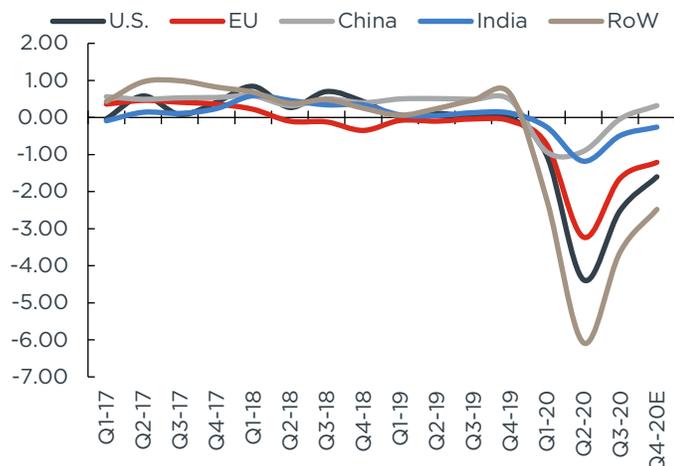
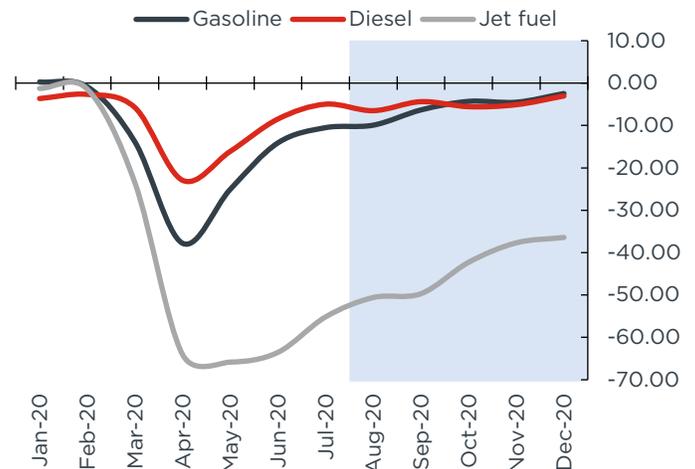


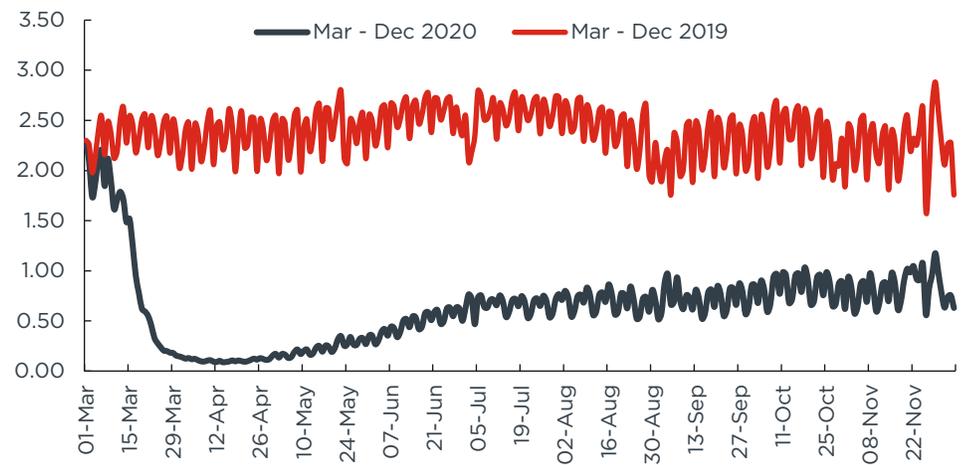
Figure 12: Refined product demand, y/y change (%)



Source: EIA, IEA, Cordros Research | Note: RoW= Rest of the World

The fall in consumption in April was focused on transport fuels, particularly jet fuel, which fell more than 60% as a result of the collapse in air travel (figure 12). Diesel consumption was the least affected transport fuel given its primary use is to transport goods by road and ships, which was less affected than air and personal car travel, although it still declined by nearly one-quarter. Gasoline and diesel have seen a relatively robust recovery as goods shipments, and passenger journeys have rebounded. While still c.10% below 2019 levels (on average) in July, we expect both to almost reach pre-pandemic levels by the end of 2020. However, we expect the weakness in jet fuel consumption to be significantly more persistent because of sharply reduced air travel.

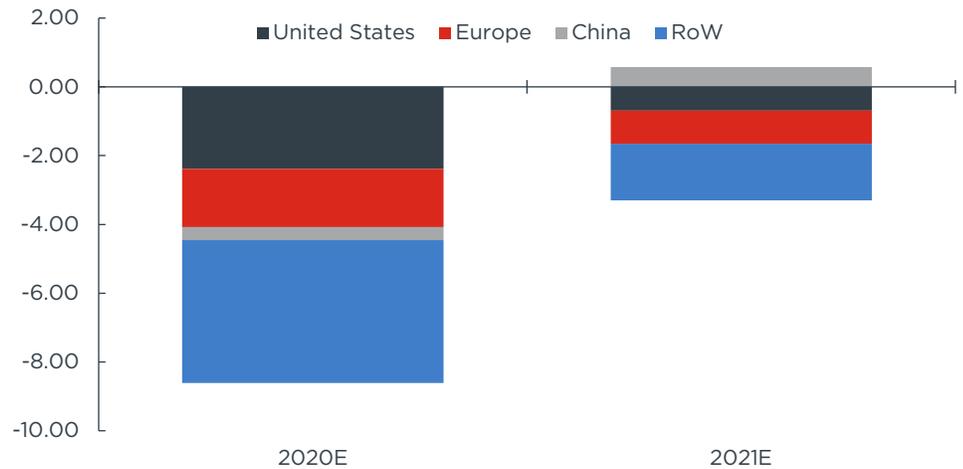
Figure 13: US TSA traveller throughput (million passengers)



Source: TSA, Cordros Research

After dropping by around 8.0% in 2020, we expect oil consumption to continue to recover in 2021, rising by 6.0%. However, it will remain 5.0% below its pre-pandemic trend (figure 14). Demand will be lower in almost all countries in 2021 than in 2019, with the notable exception of China (figure 14). According to IEA estimates, OECD demand will rise by 5.7 mb/d (-11.9%) in 2021, given the more significant impact of the virus in the US and Europe in particular, while we expect non-OECD demand to drop by 3.6 mb/d (-6.9%).

Figure 14: Oil demand forecast vs 2019 (mb/d)



Source: EIA, Cordros Research | RoW= Rest of World

Supply: Oil production declined by 5.5 mb/d (-5.5% y/y) over 9M-20. Production is now lower than consumption, which has led to a drop in inventories, although they remain at very high levels. The fall was driven by large production cuts by OPEC+ coalition, who collectively agreed to production cuts of 9.7mb/d – a reduction of more than one-fifth of their “baseline” levels – with a plan to gradually taper the cuts over the next two years (Figure 15). Compliance with the cuts so far has been high, particularly compared with previous agreements, with only a couple of countries producing significantly over their quota. The group increased production by 2.0 mb/d in August, in line with their agreed schedules.

Figure 15: OPEC+ Crude Production, y/y change (%)

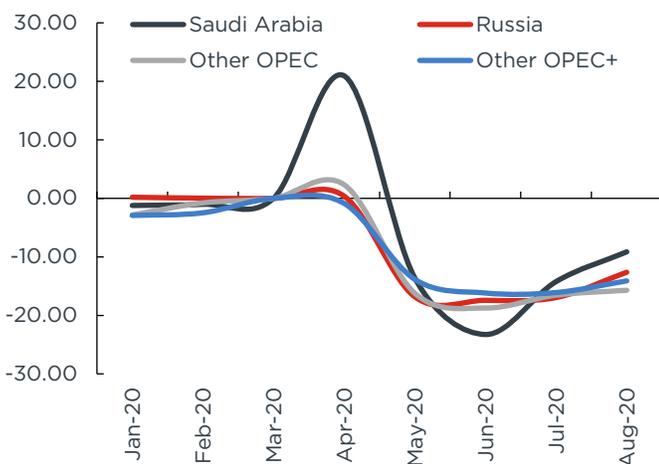
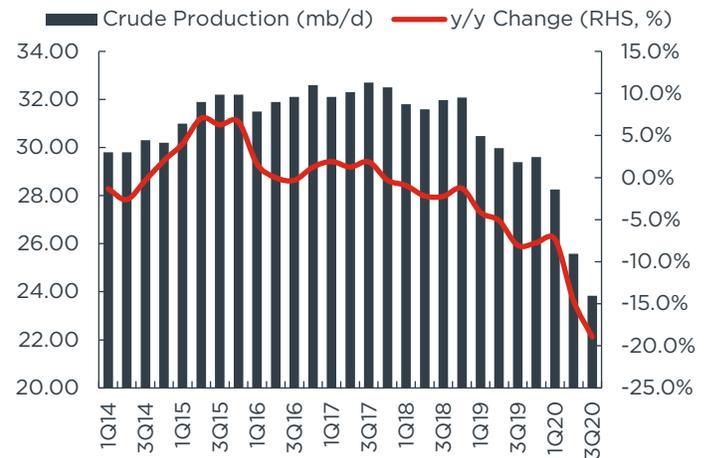


Figure 16: OPEC Crude Production



Source: IEA, OPEC, World Bank, Cordros Research

Production among non-OPEC countries has also declined rapidly, led by the United States, where production fell by 6.1 % in 9M-20. Individual producers cut production amid plummeting demand and prices, with concerns that excess

supply would overwhelm on-land storage capacity. Landlocked producers, notably many US shale producers, are particularly vulnerable to this as they are less able to access floating storage on tankers. However, while inventories rose sharply, they did not reach maximum capacity. Production in the US has since partially recovered from its trough as shale operators bring back shut-in wells in line with the recovery in demand. In Q3-20, US production averaged around 5.4% below pre-pandemic levels, although the impact of Hurricane Laura disrupted US production in August.

Instead of allowing cuts to ease by a further 2.0 mb/d from January, OPEC+, in their December meeting, agreed to a production increase of just 0.5 mb/d. They also decided to meet monthly going forward in early 2021 to assess the health of the market and decide on subsequent moves, with further monthly adjustments being no larger than 0.5 mb/d. The market expected no additional increments in production for at least the first three months of the year. Still, in our view, the group took that decision because they are anxious to recapture market share. After non-OPEC oil supply contracts by 2.5 mb/d in 2020, OPEC projects that non-OPEC supply will expand by 0.9 mb/d in 2021. But OPEC cut production by nearly 10.0 mb/d as the pandemic grew, and they are anxious to recapture some of those production cuts.

On Non-OPEC production, we expect output to rise by only 0.2 mb/d in 2021, driven by growth spread across smaller producers. However, US output is set to fall due to insufficient investment to offset declines in maturing fields and rapid depletion of shale wells. This trend is a marked difference from pre-COVID trends; between 2014 and 2019, rising US production accounted for 70.0% of the total increase in global oil production. As a result of the pandemic, we expect investment in 2020/2021 is to fall by at least 20.0%. For example, the US rig count—a measure of new drilling activity—plummeted by 77.0% y/y to reach an all-time low in August, although it has since seen a modest recovery (Figure 16). Survey results (Dallas Fed Survey) indicate that most US shale companies do not expect a significant increase in new drilling until the oil price increases above USD50/bbl. However, completion of “drilled but uncompleted wells” may be economical at slightly lower prices and could allow for a modest increase in production. Regardless, depressed new drilling, together with the rapid rate of decline of shale oil wells, we expect US production to fall by 0.3 mb/d to 11.1 mb/d in 2021.

Figure 17: US active rig count: oil rigs (units)

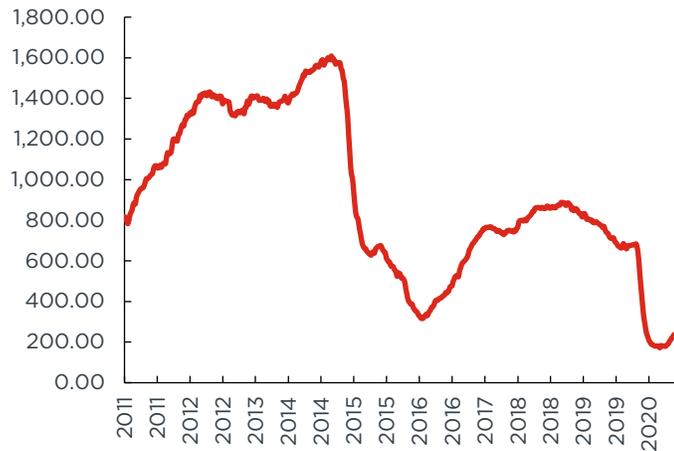
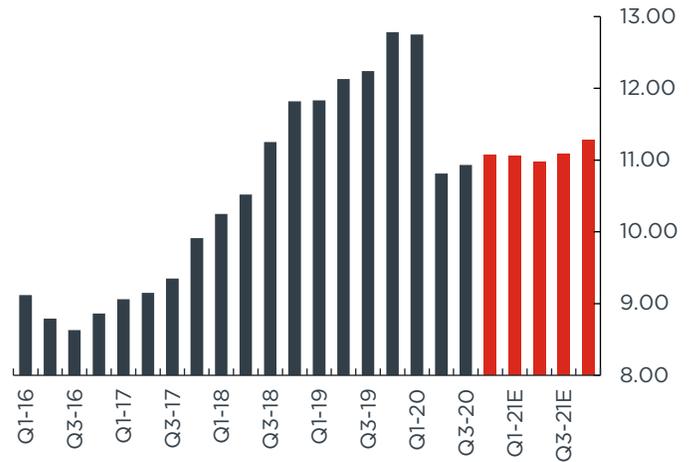


Figure 18: US Oil Production (mb/d)

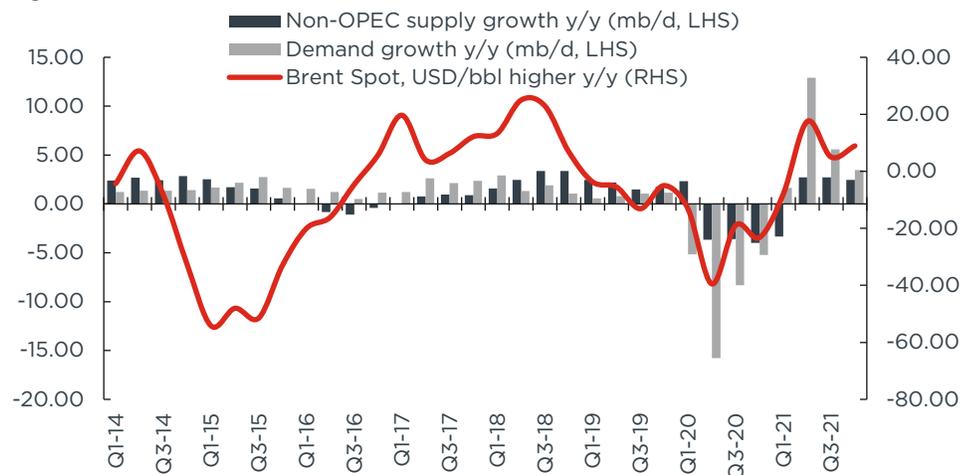


Source: Baker Hughes, EIA, Cordros Research

Price Forecasts & Risks

Considering the factors above, we forecast Brent crude price will average between USD45.00 and USD50.00/bbl in 2021. This forecast is a slight increase from a projected USD42.00/bbl for 2020E but still significantly lower than the 2019 level of USD64.16/bbl.

Figure 19: Oil Balance



Source: EIA, Cordros Research

Risks to the price forecast are tilted to the downside. The most significant risk is the duration and severity of the pandemic. An intensifying second wave in the Northern Hemisphere could lead to renewed lockdowns and reduced mobility, which would affect oil demand significantly more than other commodities. Delays to the development and distribution of a vaccine could slow the economic

recovery and risk leaving deeper scars on the global economy, further reducing oil demand.

On the supply side, production in Libya has started to recover after falling close to zero as a result of internal geopolitical conflicts (Libya's oil output averaged 1.1 mb/d during 2019). The market is also still struggling with extremely high levels of inventories which are expected to continue to unwind over the forecast and will likely keep oil prices below USD50.00 until 2022. Significant levels of spare production capacity among OPEC+ countries further reduce the likelihood of sharply higher prices.

Nigeria.

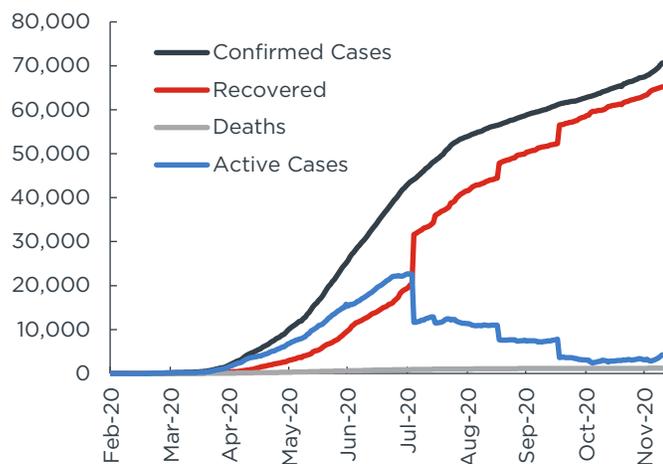
Growth.

Positive but Sub Optimal Growth Outlook

Due to the lockdown across the domestic and global economy, 2020 will go down as a historic year with a truly unique economic trajectory. Nigeria recorded its deepest GDP contraction in at least a decade in Q2 and officially slumped into its second recession in four years in Q3, as the crash in oil prices, production and trade hit output. **Overall, we anticipate that output will contract by 3.49% in 2020FY, the largest drop in nearly four decades.**

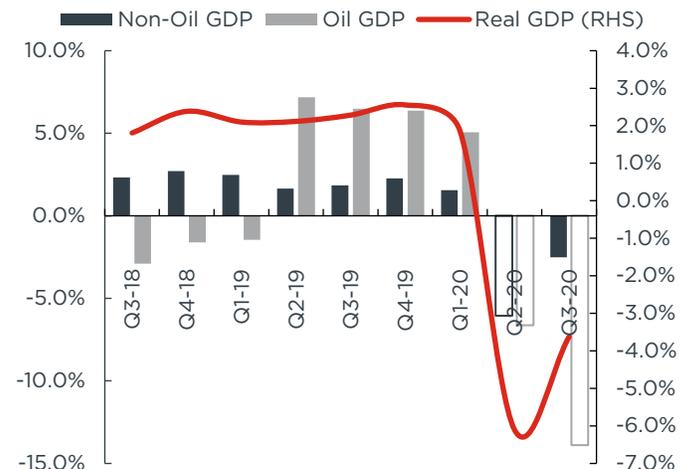
In 2021, we expect the recovery to be driven by the non-oil sector as activities in the oil sector continue to be constricted by Nigeria's compliance with OPEC+ production cuts. We expect the non-oil sector growth to be broad-based, led by the service sector, where the combination of a relatively low base and a quick rebound in economic activities is likely to improve the sector compared to 2020. We also expect the agricultural sector to remain resilient, supported by increased government intervention, while the FX liquidity challenges will continue to drag on the manufacturing sector. **Overall, we expect the oil sector to grow by 0.73% y/y and the non-oil sector to grow by 2.09% y/y. Combined, we forecast a modest GDP growth of 1.98% y/y in 2021FY.**

Figure 20: COVID-19 statistics



Source: NCDC, NBS, Cordros Research

Figure 11: Nigeria's real GDP growth

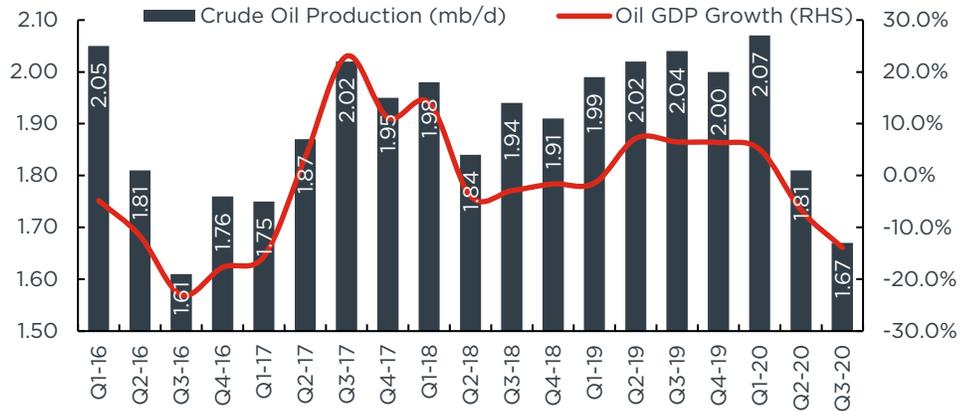


Oil Sector Growth Dampened by OPEC+ Oil Production Cuts

Nigeria's efforts to comply with its OPEC production quota resulted in crude production falling to the lowest level since the militant attacks in 2016/2017. Crude oil production declined by 10.4% and 18.1% to 1.81 mb/d and 1.67mb/d in Q2 and Q3, respectively. Consequently, Oil GDP slumped by 6.63% and 13.89% in Q2 and Q3, respectively. We note that Nigeria did struggle to meet its OPEC

mandated target of 1.70 mb/d (on our estimates, including condensates) in Q2, which led to the country taking additional cuts in Q3 to compensate.

Figure 22: Crude production (mb/d) vs oil GDP growth y/y (%)



Source: NNPC, NBS, Cordros Research

Non-Oil Sector Posted First Contraction in 11 Quarters

The twin impact of coronavirus lockdowns and the plunge in oil price hit the non-oil sector hard, with non-oil GDP posting its first contraction in eleven quarters. Non-oil GDP fell by a larger than expected 6.05% y/y in Q2-20 as activities across the manufacturing and services sectors were halted by the pandemic-induced restrictions. Following the gradual re-opening of the economy, the non-oil GDP contraction size narrowed to -3.62% y/y in Q3-20. The slightly better showing was primarily driven by a smaller contraction in the manufacturing and trade sub-sectors amidst sustained positive growth in the telecommunications and financial institutions sectors. Overall, the non-oil sector contracted by an average of 2.34% in the first nine months of 2020 (9M-19: +1.99%).

Figure 23: Non-oil GDP major components

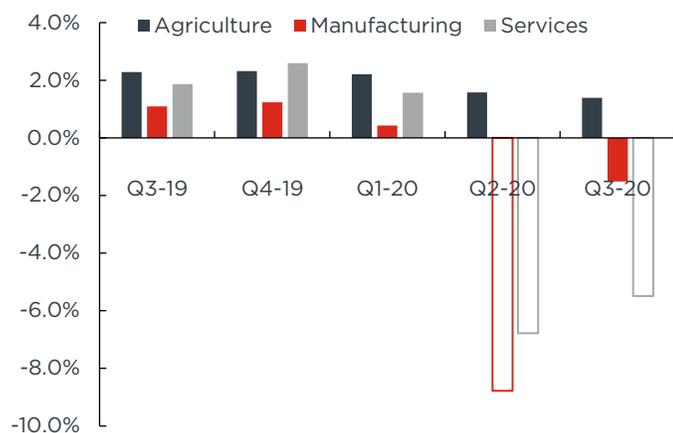
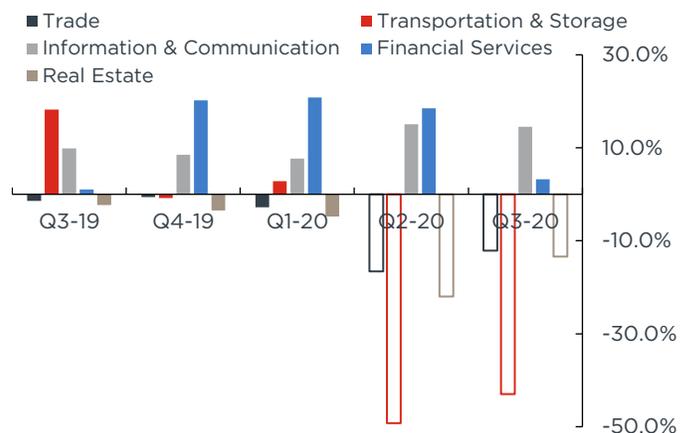


Figure 24: Services GDP major components (%)

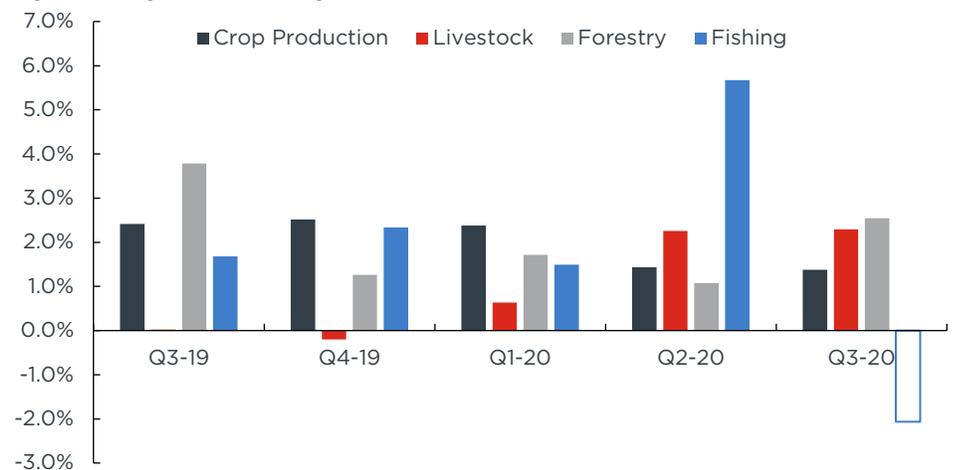


Source: NBS, Cordros Research

The Agriculture Sector Remained Resilient to Shocks

The agriculture sector remained resilient in 2020, growing by an average of 1.72% in the first nine months of 2020. Despite security challenges in food-producing regions, alongside structural barriers hindering productivity, it is pertinent to note that the agriculture sector had not contracted since 2010 when the NBS started keeping quarterly records. When the economy contracted in 2016, the sector grew by an average of 4.05% y/y. However, we note this year's outturn was the slowest growth rate for the sector since 2010. We attribute this to (1) climate change, which led to heavy rainfalls and destroyed farmland, (2) rising cases of insecurity in the food-producing regions, and (3) an underwhelming harvest season due to reduced activities during the planting season. To underscore the scale of things, growth in crop production (c.88% of Agriculture GDP) slowed to an average of 1.73% y/y in 9M-20 compared to 2.54% in 9M-19.

Figure 25: Agriculture GDP growth breakdown



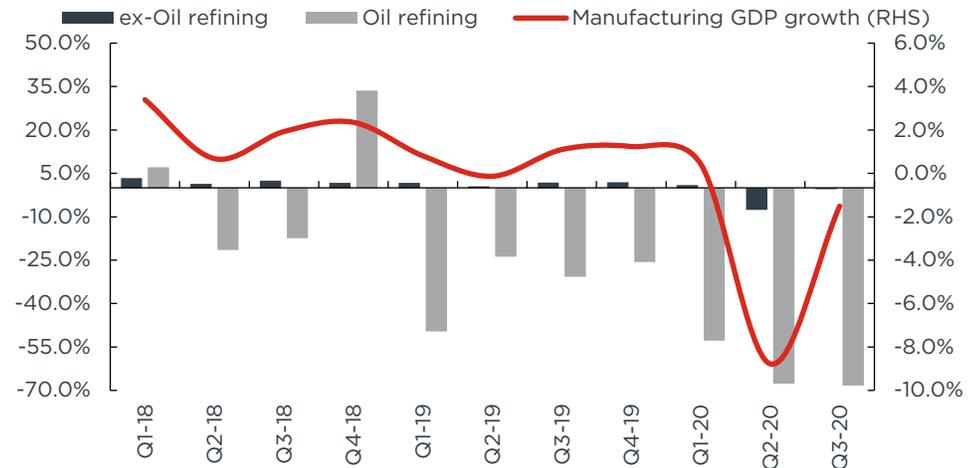
Source: NBS, Cordros Research

FX Liquidity Constraints Pressured Growth in the Manufacturing Sector

Over the first nine months of 2020, economic activities in the manufacturing sector declined by an average of 3.28% y/y – reflective of the impact of the CBN's FX demand management strategy, naira weakness, subdued demand from consumers and restriction in the movement of goods and services in the wake of the COVID-19 pandemic. We highlight that only four out of the 13 sub-components of the manufacturing sector grew compared to the previous year – the Chemical and Pharmaceutical (+3.66% y/y) and Motor vehicles and assembly (+5.01%) subsectors recorded more robust growth compared to the Cement (+2.70% y/y) and Food, Beverage and Tobacco (+1.22% y/y) subsectors.

Meanwhile, oil refining (-62.92% y/y) continued to suffer deep contractions owing mainly to the on-going rehabilitation works in the nation's refineries.

Figure 26: Manufacturing GDP Breakdown



Source: NBS, Cordros Research

Negative Outlook Maintained for Q4-20

Over Q4-20, we expect a sustained decline in the oil sector (-15.00% y/y), mostly on account of Nigeria's continued adherence to OPEC+ oil production cuts as well as the high base from 2019. Additionally, we expect the (1) weak business sentiment, (2) FX liquidity constraints and (3) the fallout from the protests which broke out in October to continue to weigh on the services and manufacturing sectors, with an overall negative impact on the non-oil sector (-6.27% y/y). **Overall, we project GDP growth of -5.61% and -3.49% in Q4-20 and 2020FY, respectively.**

Outlook: Non-Oil Sector to Boost 2021 GDP Albeit Marginally

Our growth forecast for 2021 is conservative, with our model suggesting limited upside for the oil sector but relatively stronger growth in the non-oil sector. For the oil sector, the combination of a gradual increase in crude oil production relative to 2020 and a relatively low base look set to bring the sector back to positive territory. However, our prognosis is that the non-oil sector will dictate the pace of growth over 2020. Specifically, we expect the rebound in economic activities given the favourable low base in 2020 to boost the services sector in addition to the rising activities of payment service banks in the telecommunications industry.

Figure 27: GDP growth projections(%)

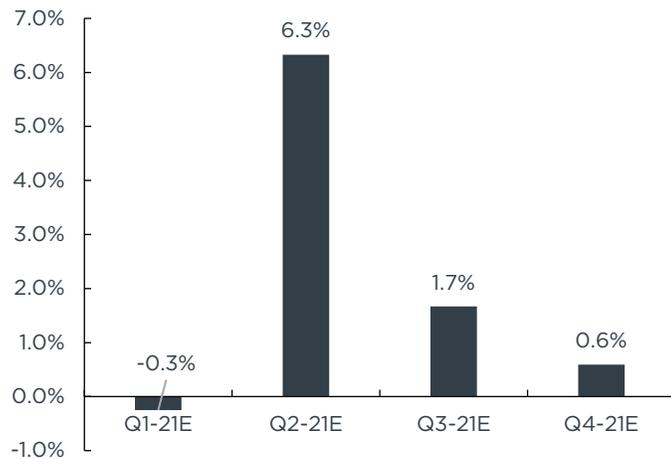
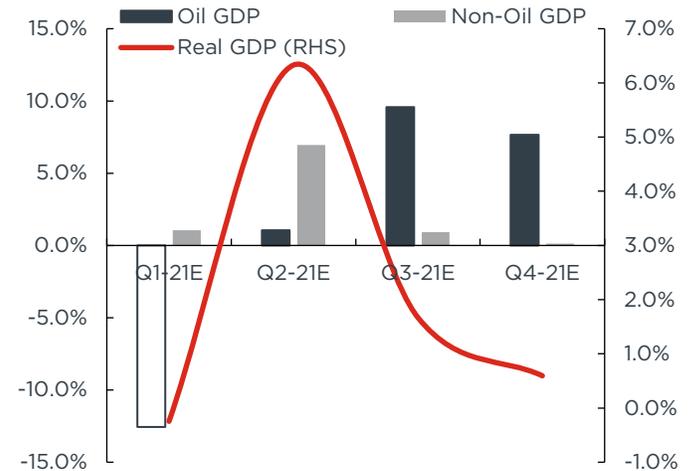


Figure 28: GDP growth by segments



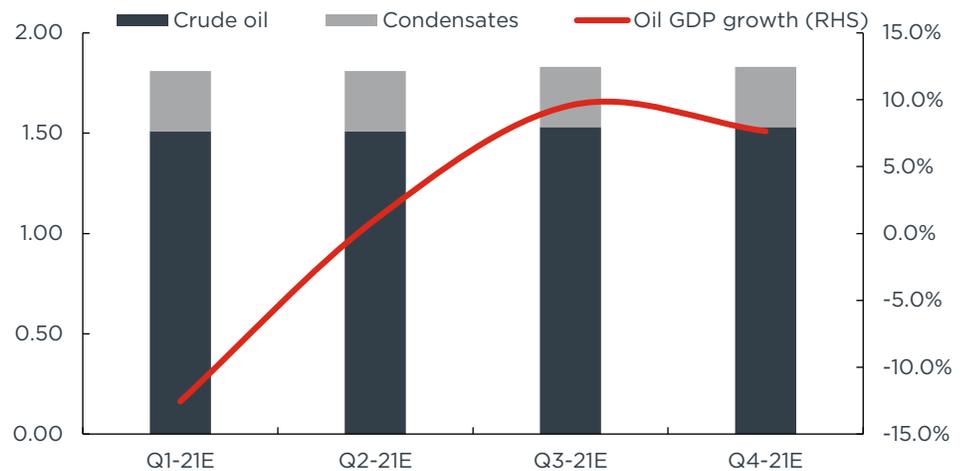
Source: Cordros Research Estimates

Oil Sector to Return to Growth on Marginally Higher Production

In the global section of our economic outlook, we stated that we foresee a rebound in global demand and trade in 2021. Specifically, with countries gradually returning to normal economic activities, we expect the demand for crude oil to increase next year. OPEC+ agreed to monthly output increases of 0.5mb/d at its last meeting, signalling some confidence in the demand recovery. This will also allow Nigeria to increase production slightly by about 22kb/d, according to Bloomberg estimates. Given that Nigeria over-complied with the OPEC+ cut agreement in October and November, we estimate that the country is now only owing OPEC 35kb/d in compensation, which we expect will make up in December.

Consequently, the new agreement will allow Nigeria to increase crude oil production to 1.52mb/d (excluding condensates) starting from January. We are also confident that the FGN's peace deal with the militants and various stakeholders in the Niger-Delta region will remain intact. Against this backdrop, we estimate the average oil production (inclusive of condensates) of 1.83mb/d, implying oil GDP growth of 0.72% y/y in 2021FY.

Figure 29: 2021 Oil production vs GDP

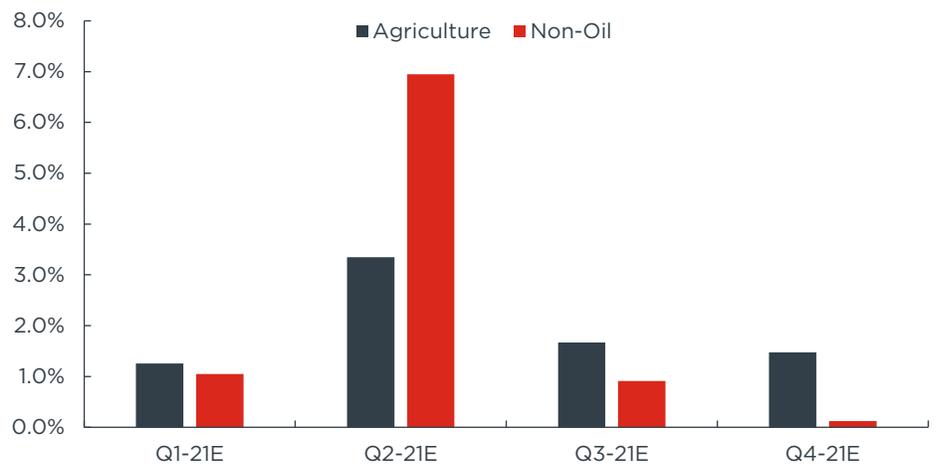


Source: Cordros Research Estimates

Agriculture Sector to Remain Resilient in 2021

We expect the downward pressure on the agriculture sector output to persist. However, we believe the (1) increased free movement of farmers, (2) gradual adoption of climate-smart agriculture practices (treating dry and wet season the same way) and (3) government initiatives towards boosting output in the sector will ease these pressures slightly. For example, the CBN introduced the Accelerated Agricultural Development Scheme (AADS) and seven other intervention schemes for the agricultural sector to increase food security and economic diversification. Similarly, in a bid to reduce post-harvest losses of farmers, the FGN requested the approval of the National Assembly to obtain a USD1.20 billion loan from Brazil. In modelling our growth expectation for the sector in 2020, we discounted our expected output growth by several identified downside risk factors, including (1) herders/farmers conflict/banditry, (2) poor farming practices and low-quality seedlings, and (3) flooding in the food-producing states. **On a balance of risks, we expect the Agriculture sector's growth to print 1.89% in 2021.**

Figure 30: Agriculture GDP growth



Source: Cordros Research Estimates

Services Sector Growth Hinged on Telecoms Performance

We expect the relaxation of stiff restrictions to continue supporting recovery in the services sector, with the telecommunications sector being at the forefront of growth. On the positives, we expect concerted efforts by telecommunication companies in driving internet penetration and CBN’s approval of Payment Service Banks (PSBs) to sustain the impressive growth in the ICT sub-sector. For clarity, the CBN has granted approval in principle for Unified Payment’s Hope PSB, 9Mobile’s 9PSB and Globacom’s Money Master to operate Payment Service Banks. Consequently, we expect the growth in the mobile money space to support the sector. However, the magnitude of the increase may not match that of 2020 due to the high base effect and as people return to work, which will reduce data usage.

That said, we note that there are specific sub-sectors in the services sector that we expect to remain under pressure. For example, in the real estate sub-sector, we expect the declining purchasing power of consumers and increased cost of living to affect demand for capital goods, offsetting the positive impact of reduced borrowing costs in property development. Similarly, we expect adverse trade policies such as the FX illiquidity challenges, and decrepit infrastructure at the ports and weak distribution networks to constrain growth in the trade sector. **Overall, we modelled telephone and internet subscribers to grow by an average of 6.2% y/y and 10.6% y/y, respectively. Overall, we expect the service sector to grow by 2.69% y/y in 2021.**

Figure 31: ICT and Services GDP growth

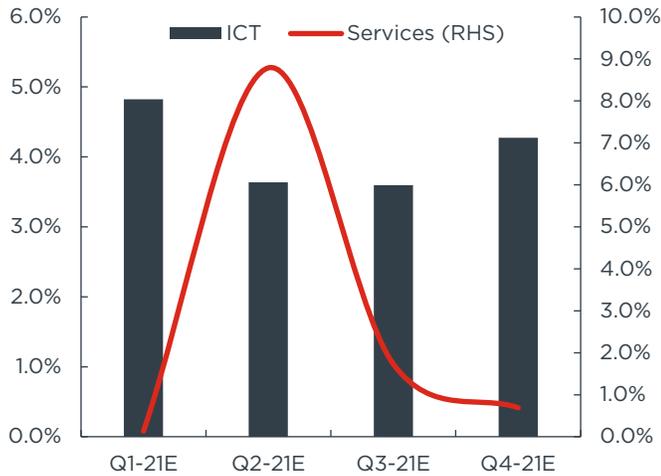
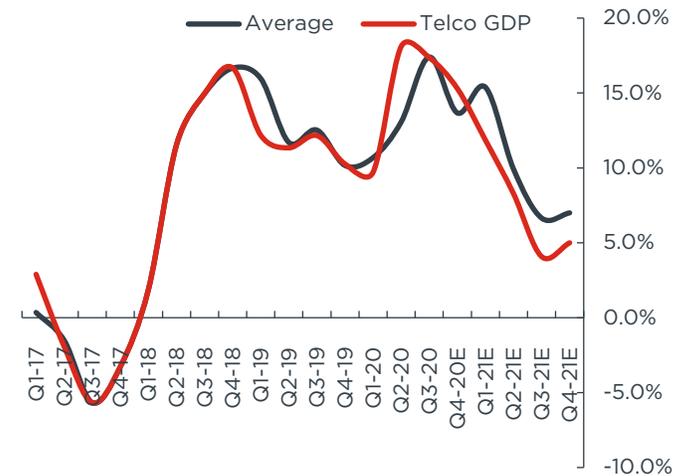


Figure 32: Average growth in callable minutes/internet subscription and Telco GDP



Source: NCC, NBS, Cordros Research

FX Illiquidity, Structural Bottlenecks to Hinder Manufacturing Growth

On our expectation that Brent crude oil will average between USD45-USD50/bbl in 2021, we expect the CBN to continue with its FX demand management strategy to manage the external reserves. This strategy, alongside subdued demand from consumers and pre-existing bottlenecks in the operating environment, should inhibit growth in the sector. **Based on the preceding, we expect the manufacturing sector's weakness to continue over 2021, and thus, forecast a negative growth of 0.89% y/y.**

Figure 33: Manufacturing GDP Growth

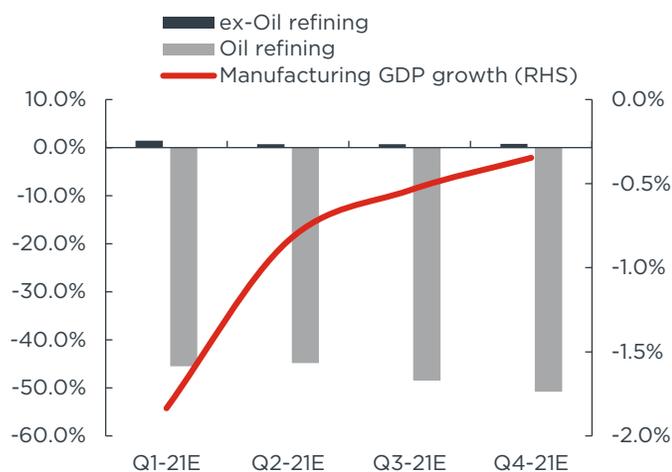
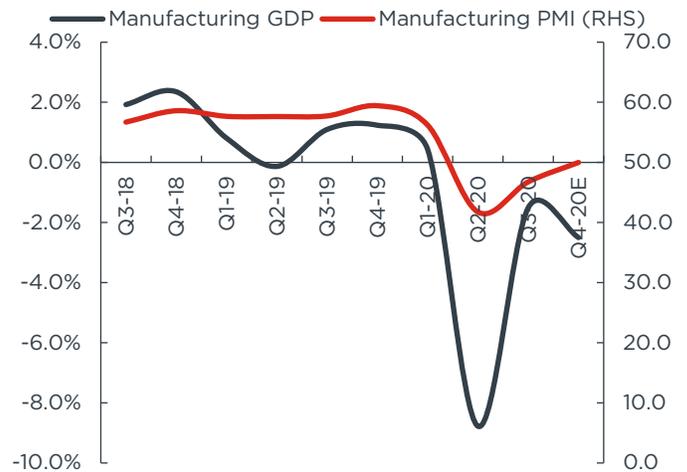


Figure 34: Manufacturing PMI vs Manufacturing GDP



Source: NBS, CBN, Cordros Research Estimates

Having modelled our expectations across both the oil and non-oil sectors, we expect full-year growth of 1.98% y/y in 2021 (2020E: -3.49% y/y).

Inflation.

Inflationary Pressure to Persist Over 2021

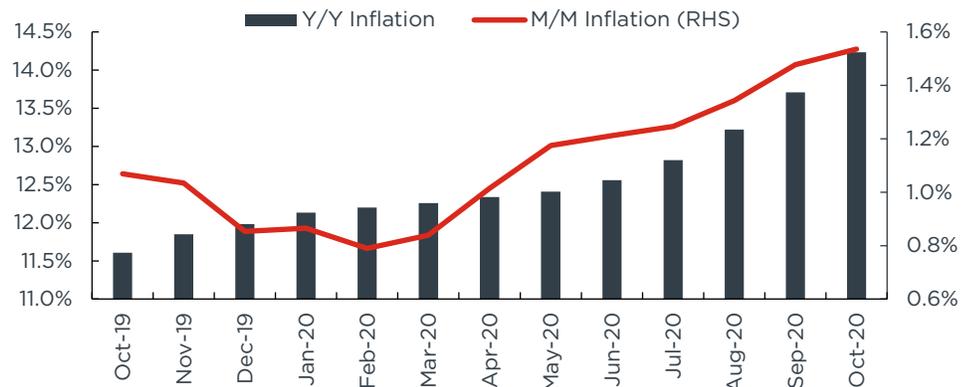
The uptrend in consumer prices, which began in September last year, following the border closures, intensified in 2020. To the monetary authorities' chagrin, headline inflation moved further away from the CBN's 6%-9% target; it surged to a 32-month high in October on rising food prices caused by border closures, dollar restrictions and banditry attacks that prevented farmers from producing food.

Analysing several factors that may shape domestic prices in 2021, we expect inflationary pressure to persist next year. **Our base-case scenario suggests headline inflation will average 16.65% y/y in 2021, the highest level since 2016, with the year-end figure printing at 15.43% y/y.** We hinged our forecast on our expectations for (1) a gradual increase in electricity tariffs as service delivery improves, (2) a depreciation of the currency to NGN425/USD, and (3) the re-opening of the land borders.

Headline CPI Firmed up in 2020

Headline inflation in 2020 faced upward pressure from both the food and core baskets. On food prices, (1) the continued border closure, (2) resultant effect of heavy rainfall on farmlands, (3) limited movement during the planting season on the harvest, and (4) COVID-19 induced supply chain disruptions put pressure on food inflation. On the core basket, we attribute the rise to (1) the increase in VAT from 5.0% to 7.5%, (2) the depreciation of the currency, (3) the partial liberalisation of the downstream sector, and (4) the power sector tariff increases. The perfect storm of factors pushed headline inflation higher by 225bps to 14.23% y/y between January and October. Food inflation rose by 271bps to 17.38% y/y during the review period, while core inflation increased by 181bps to 11.14% y/y.

Figure 35: Historical y/y headline inflation



Source: NBS, Cordros Research

Inflationary Pressure to Persist in 2021

In forecasting Nigeria's headline inflation rate, we analysed various factors that may shape the domestic prices over 2021, which include but are not limited to:

- Persisting FX supply constraints
- Electricity tariff hikes
- Naira devaluation
- Market determined fuel prices
- Land border closures

FX supply: In 2020, the CBN's FX demand management strategy had spillover effects on importing raw materials for production. As such, we believe the impact of the FX supply challenges has permeated into higher domestic prices. Although we expect the FX supply challenges to linger in 2021, we do not expect the impact to be as pronounced as 2020.

Electricity tariffs: After suspending implementing the service-reflective electricity tariff for three weeks, the NERC (based on the joint agreement between the organised labour and the FGN) asked the power Distribution Companies (Discos) to begin the implementation of a revised electricity tariff starting from November 2020. We note that the updated tariff was revised downwards compared to the initial hike across most service bands.

Naira devaluation: We expect a further devaluation of the currency in 2021 based on our expectation of limited dollar inflows amid rising demand for FX to meet external obligations.

Market determined fuel prices: We expect crude oil prices to average between USD45.00 and USD50.00/bbl. Consequently, we expect PMS prices to remain rangebound (NGN165-NGN175/litre), especially with the N5.00 implicit subsidy recently announced by the government. However, risks to PMS prices are tilted to the upside as a devaluation of the currency would drive prices higher (as long as oil prices don't fall). An increase in PMS prices would negatively impact transport prices.

Land border closures: The uptrend in inflation begun when the borders were shut in August 2019, a phenomenon that continued through 2020. Food prices hit a 32-month high in October, escalated by Covid-19 induced supply chain disruptions. Hence, we are of the view that the recent re-opening of the borders will help in easing food price pressures over 2021.

Based on the preceding, we modelled three (3) scenarios for the headline inflation in 2021:

Figure 36: Headline inflation (y/y) scenarios

	Base Case	Bull Case	Bear Case
<u>Factors</u>	<u>Expectation</u>	<u>Expectation</u>	<u>Expectation</u>
Higher Electricity Tariffs Maintained	Yes	No	Yes
Currency Devaluation	I&E Window depreciates to NGN415/USD	I&E Window stable at NGN395/USD	I&E Window depreciates to NGN440/USD
PMS Price (NGN/litre)	NGN170	NGN165	NGN175
Border Closure	Land Borders are re-opened	Land Borders are re-opened	Land Borders remain closed throughout 2021
Inflation (2021 Avg.)	16.65%	14.73%	17.25%
Inflation (2021 Year-end)	15.43%	14.11%	17.52%

Source: Cordros Research Estimates

Balance of Payments.

External Position to be Deteriorate Further in 2021

Nigeria’s already dire external account picture was worsened by the effects of the pandemic as exports slumped, offsetting the slower decline in imports, and capital inflows weakened. Total exports declined by 37.5% in H1-20 due to lower oil receipts, which constituted c. 83% of the total exports. Imports declined slower by 17.8% on account of the lockdown embarked upon by advanced economies and the FX management strategies of the CBN. Elsewhere, remittances (c. 88% of total current transfers) declined sharply by 33.1%, resulting in a current account deficit of USD8.86 billion (H1-19: USD7.36 billion deficit).

Over 2021FY, we expect the Current Account (CA) deficit to widen to a record high. This is hinged on our expectation of increased import demand as the domestic economy improves and a slower increase in exports. We also expect pressure in the service account following the gradual recovery of global services and tourism. **Overall, we expect the CA deficit to sit at USD22.63 billion in 2021FY, which translates to an absolute CA balance of 4.57% as a percentage of GDP**

Capital Controls and Global Lockdown not Enough to Outturn Weak External Position

In Q2-20, Nigeria’s CA balance recorded its eighth consecutive quarterly deficit, declining by 42.6% q/q. We note that the total CA deficit of USD3.23 billion translates to 3.4% of GDP (Q1-20: 4.9%). Analysing the breakdown, we highlight that the 36.4% q/q decline in current transfers (USD3.91 billion), the lowest since the CBN started keeping data in 2008, primarily influenced the negative outturn.

Figure 37: Goods, Service, Income, Current transfer (USD’ billion)

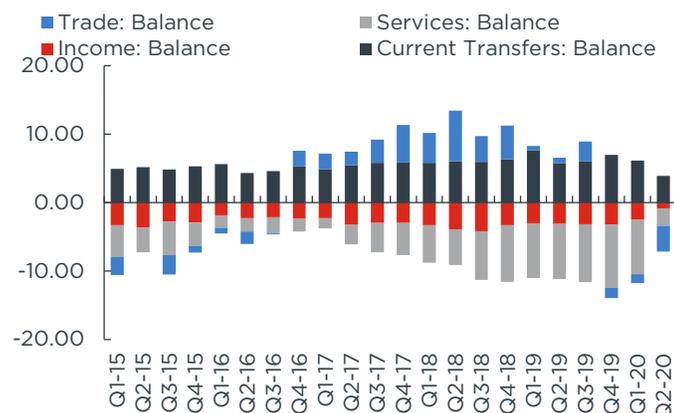
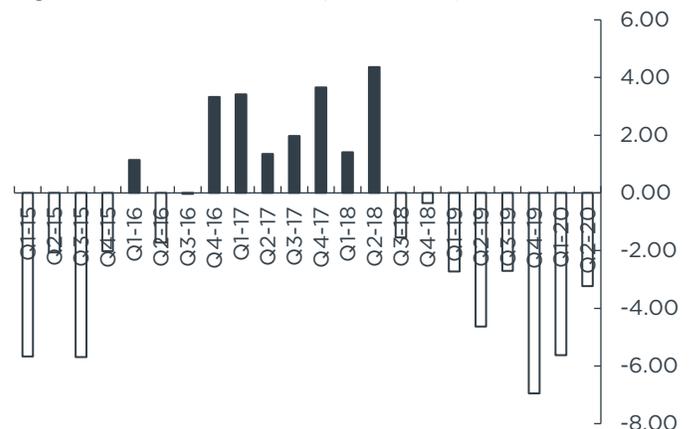


Figure 38: Current Account (USD’ billion)



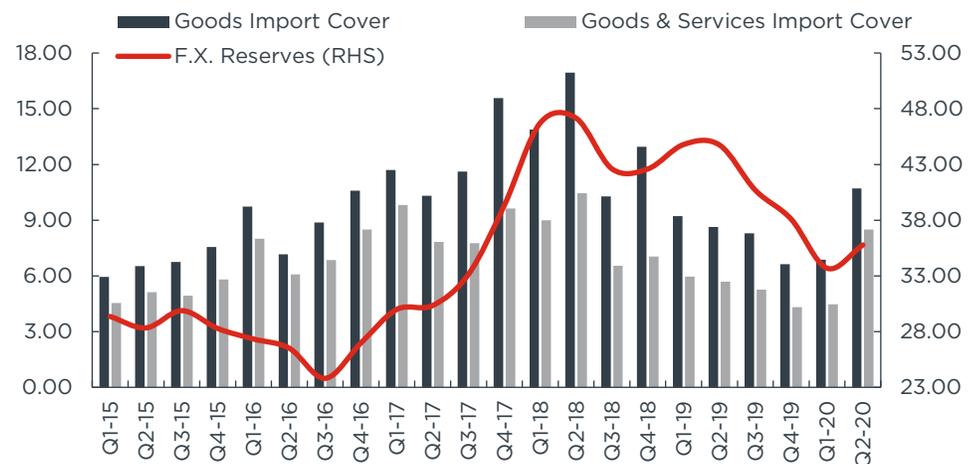
Source: CBN, Cordros Research

The fall in current transfers was due to a 40.1% q/q decline in workers' remittances. The trade deficit also widened to USD3.74 billion (+181.4% q/q), the highest since at least 2008 as exports (-52.7%) fell faster than imports (-31.6%). The deterioration in remittances, together with the negative trade balance, was enough to offset the decline in services (-67.6% q/q) and income payments (-66.9% q/q).

Current Account Deficit to Deteriorate to the Highest Level on Record

For 2021, we modelled a 0.6% y/y increase in oil exports on the back of improved crude oil prices. Thus, total inflows from exports are expected to settle at USD36.16 billion (2020E: USD35.96 billion). Assuming the CBN's current capital controls remain in place, we project outflows for imports will fall by 7.2% y/y in 2021 to USD40.09 billion (2020E: USD43.20 billion). **Hence, the trade deficit is expected to decline by 45.7% y/y to USD3.93 billion, majorly due to the FX liquidity challenges, which will reduce goods and services imports compared to marginal growth in exports.**

Figure 39: FX Reserves (USD' billion) and Goods and Services Import Cover



Source: CBN, Cordros Research estimates

Similarly, with the gradual recovery of travel and tourism, we expect pressure in the service account as the people travel more. This is likely to weigh on the demand for foreign currencies for service-based transactions. As a result, our model suggests the services account (net) will increase by 35.7% y/y in 2021 while net income payments will also increase, to USD12.06 billion (2020E: USD9.15 billion), due to the increase in income payments on account of investment income. Elsewhere, the resumption in economic activities would mean that workers return to work, translating to improvement in remittances. **As a result,**

we expect the net current transfers to improve by 10.8% y/y to USD22.13 billion (2020E: USD19.97 billion) – 16.1% less than the pre-COVID level.

The land border closures reduced imports into the country; however, we note that its impact on the overall current account has been muted. Trade through the land borders only constitutes an average of c.5% of the total payments for imports. Specifically, the total imports using Informal Cross Border Trade (ICBT) was USD2.64 billion and USD2.31 billion in 2018FY (6.5% of total imports) and Q1-Q3 2019 (5.1% of total imports), respectively. Consequently, with the re-opening of the land borders, our model suggests that the CA deficit will settle at USD22.63 billion, which is 28.5% greater than our projected CA deficit of USD17.61 billion in 2020FY. This translates to a CA deficit as a percentage of GDP of 4.57% (2020E: 4.02%) at an effective exchange rate of NGN380.00/USD. However, the current account pressure may force the CBN to devalue the currency at the official window to NGN400/USD, which will translate to a CA deficit of 4.81% of the GDP.

Figure 40: Trade Balance Historical and Forecast (USD' billion)

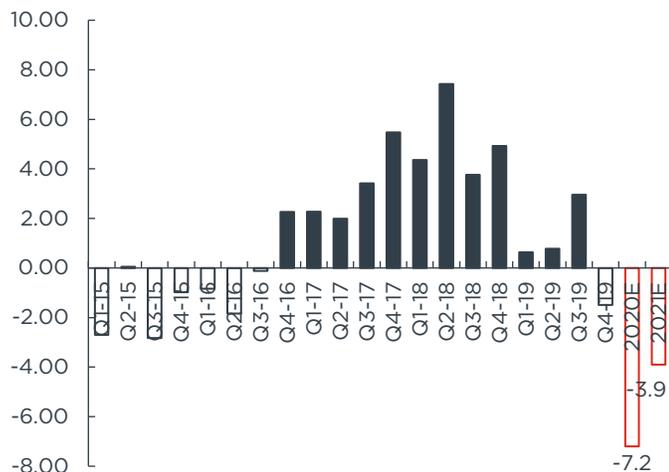
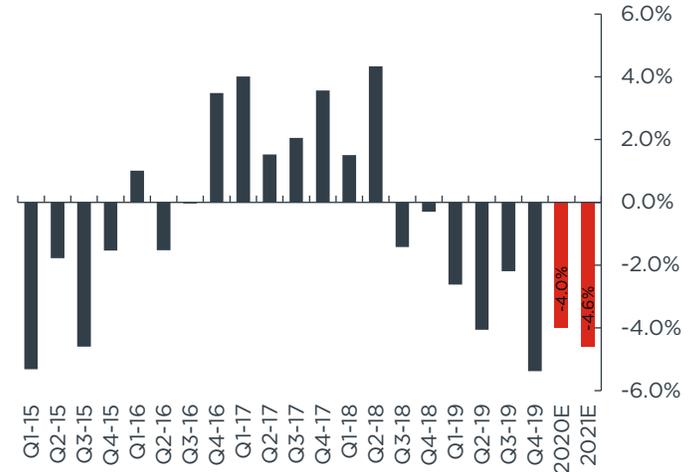


Figure 41: CA Balance (as a % of GDP)



Source: CBN, Cordros Research Estimates

Currency.

Currency Stability by Strangulation

Over the first ten months of 2020, the naira faced its first real test since introducing the I&E window (IEW) in April 2017. Although the currency was relatively stable at the start of the year, the COVID-19 induced decline in oil prices worsened the already fragile balance of payments (BOP) picture, forcing the CBN to adjust the currency at both the official and I&E windows. Pertinently, the CBN devalued the currency by 23.5% at the official window to NGN379.00/USD, while the IEW rate depreciated by 9.7% to NGN395.00/USD. **However, the naira continues to trade above our Real Effective Exchange Rate (REER) estimate of NGN453.67/USD at the parallel market. The low greenback liquidity at the official window has increased demand in the parallel market, driving the rate to as high as NGN475.00/USD as of 11th December 2020.**

Despite the two-step depreciation at the official window, we believe the naira is grossly overvalued. By 2021, our gloomy view on the fundamental picture also leaves little to cheer. We expect Nigeria’s current account deficit to widen to USD22.63 billion or 4.3% of GDP in 2021E. This, alongside our expectations of subdued capital inflows, on account of FX liquidity challenges amid low yields on OMO bills, should leave the CBN at the mercy of the FX reserves to support the naira, in our view. **Overall, we expect the naira to depreciate closer to its fair value implied by long-run REER (NGN453.67) in 2021FY, given the expected pressure on the external reserves amid weak portfolio inflows. Our baseline expectation is that the CBN will depreciate the naira by 5.3% to NGN400/USD in the interbank market and 5.1% to NGN415/USD at the IEW.**

Figure 42: IEW vs Parallel Market Rates (USD/NGN)

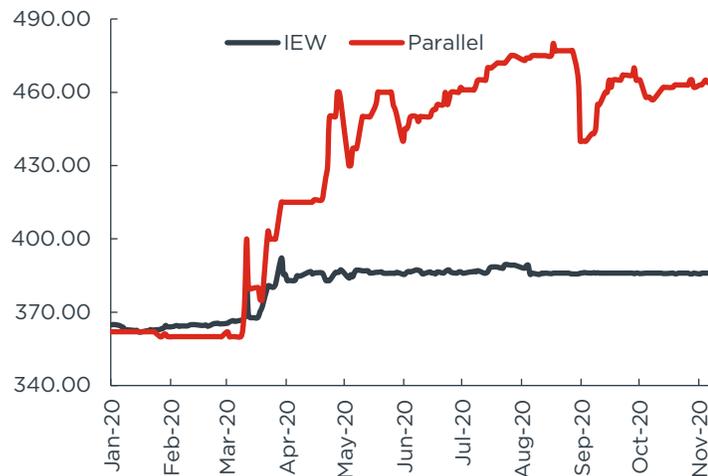
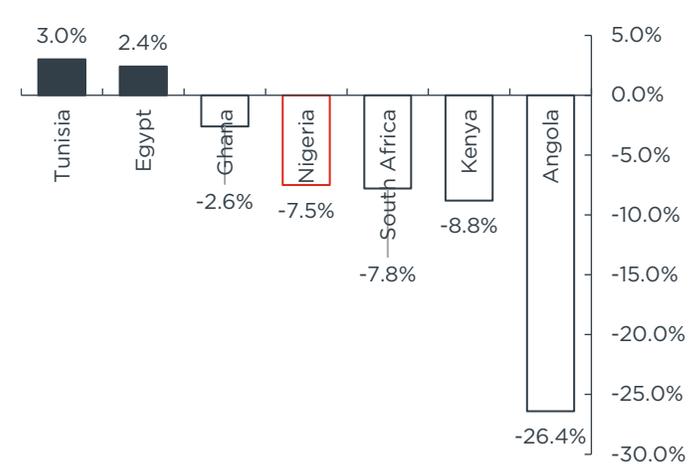


Figure 43: African Currencies, YTD return (%)



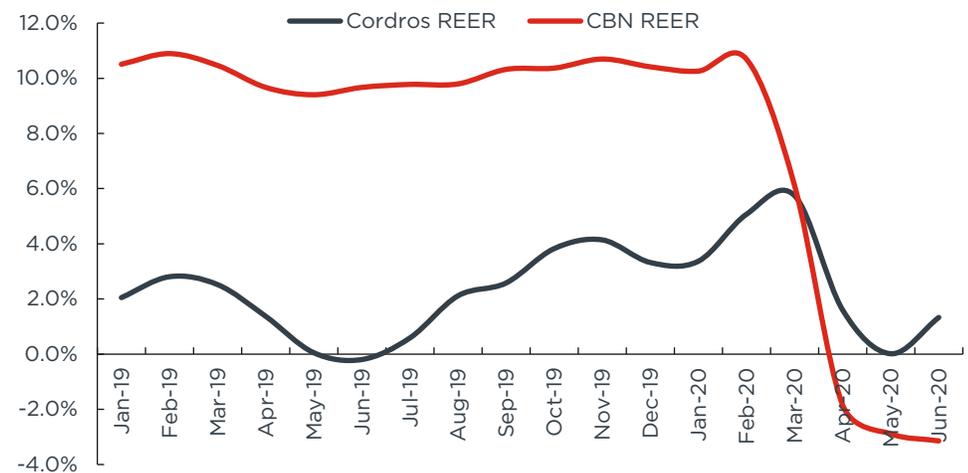
Source: Bloomberg, AbokiFX, Cordros Research

How Overvalued is the Naira at Current Levels?

During periods of economic downturn, a managed exchange rate regime is considered optimal compared to a floating one due to increased volatility in capital flows as investors move towards safe-haven assets. However, the current devaluation level is not tenable as sub-optimal devaluations further create market distortions and instability in the financial markets. For instance, a sub-optimal devaluation increases the rate of speculation as market participants hold on to foreign currencies in expectation of further devaluation. The differential (19.2%) between the NAFEX and parallel market rates, which is greater than the 2.0% IMF divergence guideline, is evidence of this.

In nominal terms, our analysis suggests that the naira is indeed grossly overvalued at current levels, with fundamentals dictating a rate of NGN453.67/USD in the open market. Our model shows that the current USD/NGN rate should depreciate by 19.4% and 14.9% using the interbank exchange rate and the IEW rate, respectively, if the naira were fairly valued. However, currencies hardly ever trade at their fair values in the short term due to varying fundamental issues.

Figure 44: Fair Value of the Naira



Source: CBN, Cordros Research estimates

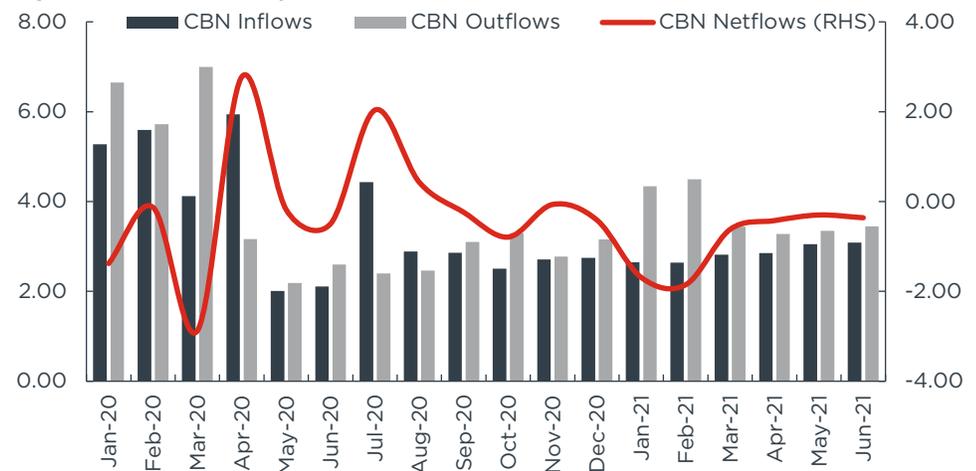
Covering All Bases

In estimating how long the CBN can sustain its FX rationing, we forecast the CBN's liquidity position for H1-21 while taking into cognisance the FX reserve drawdown to service the current account deficit. On the liquidity position, our crude oil price and production estimates translate to average monthly oil inflows of USD939.00 million (-17.4% y/y) over the first half of 2021.

Similarly, developments in non-oil inflows are not encouraging as foreign investors prefer to wait on the sidelines till FX liquidity issues are resolved. Thus, the CBN's ability to accumulate FX reserves through the IEW, as it did pre-pandemic, has been undermined. As a result, we project average monthly non-oil inflows will plunge by 37.1% y/y to USD1.91 billion over the first half of 2021. **Overall, the total inflows into the CBN's coffers (excluding Eurobond issuance) are expected to average USD2.85 billion monthly over the first half of 2021 (H1-20: USD4.17 billion).**

Elsewhere, given the unimpressive domestic macroeconomic landscape and the FX liquidity challenges, we expect FPI inflows to remain tepid. At the same time, the CBN's FX demand management strategy will keep the outflows in check. A total of USD10.01 billion worth of OMO bills will mature in H1-21, with c.45% (USD4.50 billion) estimated as the foreign portfolio portion of the total maturing bills. We assume that c.35.0% of this foreign portion will not be rolled over by investors, implying average monthly capital repatriation of USD262.52 million. The re-opening of the land borders is however expected to increase the CBN's US dollar sales for eligible imports. **Thus, we expect the CBN's average monthly cash outflow to decline by 18.7% y/y to USD3.70 billion.**

Figure 45: CBN's Monthly Cashflows (USD' bn)



Source: CBN, Cordros Research

On balance, we estimate an average monthly reserve drawdown of USD851.66 million (vs average monthly drawdown of USD386.56 million in H1-20). Overall, we estimate the FX reserves will settle at USD29.84 billion by June 2021, translating to a goods and services import cover of 6.8x (7 months), just above the IMF's six months minimum requirement for the West African Monetary Zone (WAMZ). With the inclusion of a possible Eurobond issuance (est. USD2.5 billion), we expect the reserves to settle above USD32.00 billion.

The BOP situation, however, provides a downside risk to the accumulation of the reserves. The currency will continue to face a lot of pressure amid the current account balance's dire state as travel and trade pick up. The FX futures contracts also paint a picture around this. FMDQ quoted the 6-month and 1-Year contracts at NGN413.48/USD and NGN431.08/USD, respectively, as of 4th December 2020. **Therefore, the possibility of another devaluation remains high. Our baseline expectation is that the CBN will depreciate the naira by 5.3% to NGN400/USD at the minimum in the interbank market, and 5.1% to NGN415/USD at the IEW.**

Figure 46: CA Balance vs FX Reserves (USD billion)

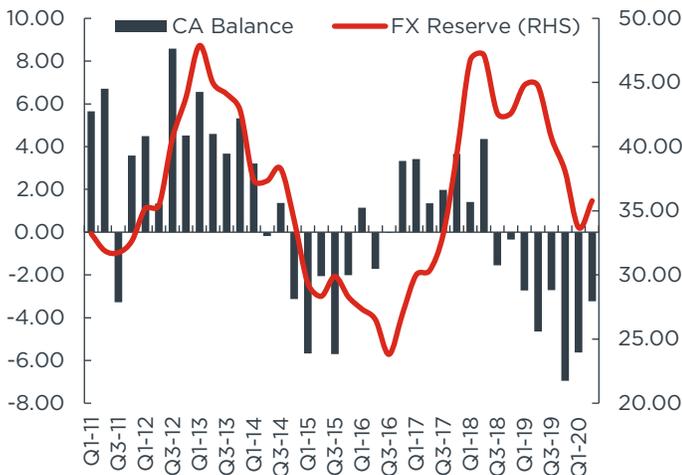
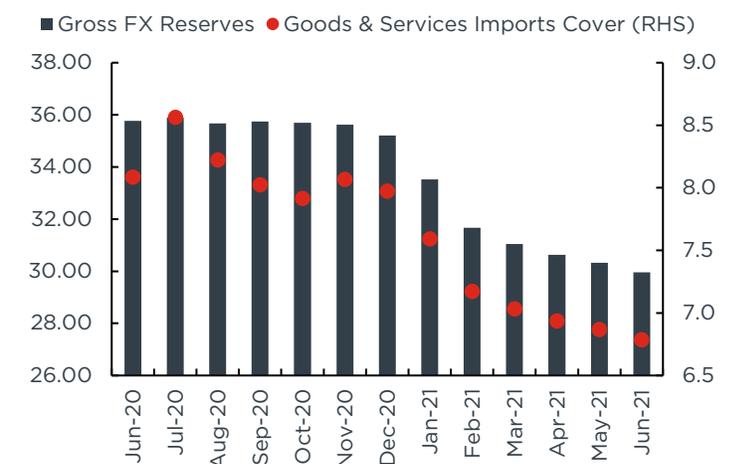


Figure 47: FX reserves (USD billion) and import cover (months)



Source: CBN, Cordros Research Estimates

Monetary Policy.

The MPC Will Be at Crossroads in 2021

In our 2020 mid-year outlook, we expressed our view that the trajectory of economic growth and the exchange rate will be central to our outlook for the MPC. True to our prognosis, the MPC leaned more towards supporting economic growth and opted for unconventional policy actions, given the decline in output induced by the pandemic. Except for January when the MPC raised the CRR by 50bps to contain the elevated banking system liquidity, the committee's decisions in subsequent meetings were largely accommodative.

Our base case expectation for 2021 is that monetary policy will remain dovish in the short term, particularly in Q1-21, where we expect the MPC to remain unchanged. In our view, however, monetary policy tightening is inevitable from Q2-21, underpinned by our expectations of (1) economic growth turning positive and (2) sustained inflationary pressure - we expect continued pressure in the food basket coupled with energy price shocks (higher PMS and power costs). **Consequently, we expect the CBN to hike the MPR by 50bps in Q2-21 with the possibility of another 50bps hike in H2-21. Nonetheless, we believe the pace of tightening will be dependent on the external sector conditions.**

Figure 48: MPR & Inflation

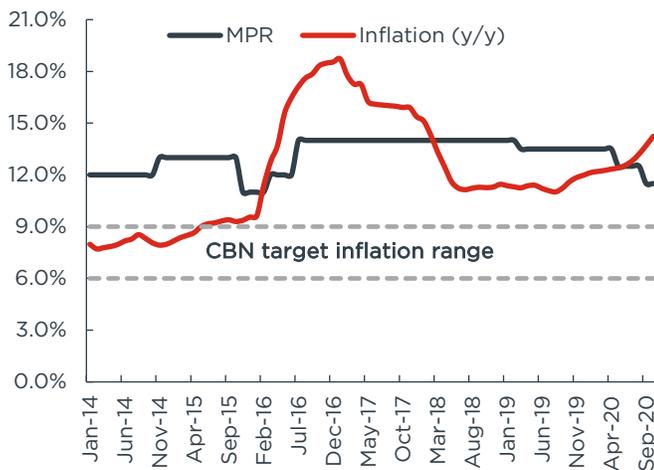


Figure 49: Food Inflation (m/m)



Source: NBS, Cordros Research

Unorthodox Policies Persist as Economic Growth Takes Precedence

The CBN justified its dovish stance because current inflationary pressures are being driven by supply-side factors outside the confines of monetary policy. Consequently, the bank exhibited a great deal of tolerance for elevated system liquidity, which pressured yields downwards. Accordingly, the average yield on

local currency government bonds crashed to 4.1% (as of 4th December), from 10.8% at the start of 2020, despite the country’s widening fiscal deficit and spiralling inflation. Similarly, OMO instruments yields plummeted significantly at the primary auctions to an average of 5.2% in November compared to 12.8% at the auction in the corresponding period of 2019.

Compared to other developed and emerging markets central banks, the MPC was late to the “party of the doves” (the MPC first cut rate in May compared to the sweeping cuts seen across the globe in March/April). However, the committee noted that traditional monetary policy tools’ weak transmission mechanism led to increased reliance on unorthodox policies – intervention loans, segregation of the OMO and T-bills market, and the loan-to-deposit (LDR) ratio directive – in influencing macroeconomic outcomes. In response to the global pandemic, the CBN looked to several policy measures, including (1) the launch of a NGN3.50 trillion stimulus program, (2) maintaining the 65.0% loan-to-deposit ratio, (3) lowering the rates on intervention loans to 5.0% from 9.0%.

Figure 50: OMO Net Inflows (NGN billion)

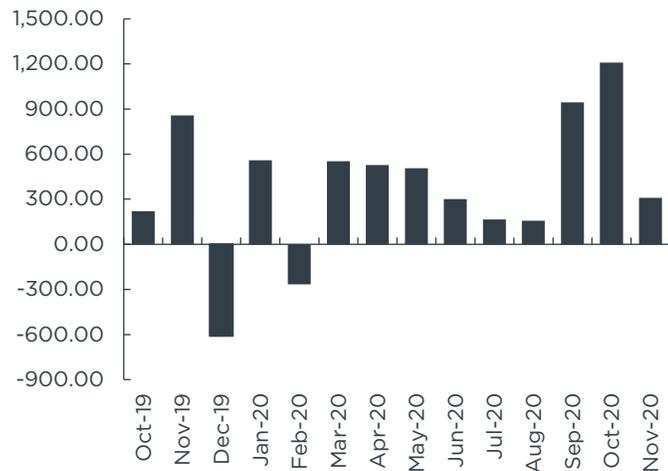
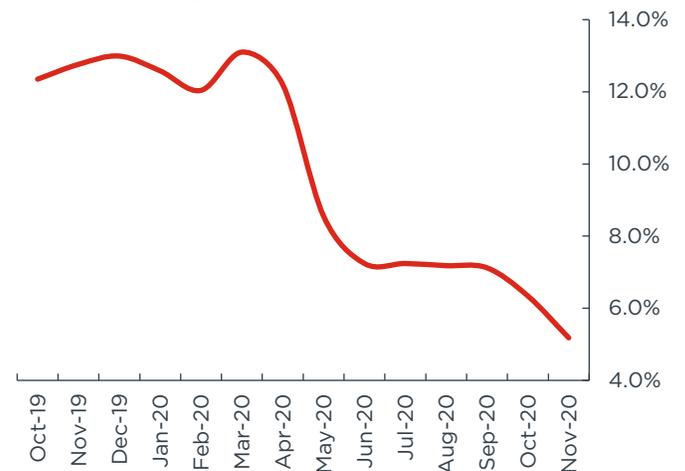


Figure 51: Average OMO stop rate (%)



Source: FMDQ, CBN, Cordros Research

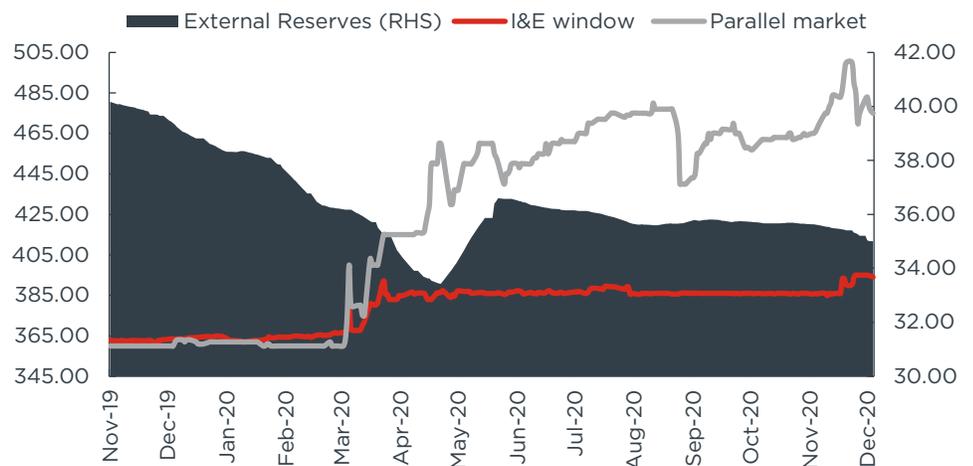
Policy Trilemma: Capital Flows as the Sacrificial Lamb

The theoretical basis behind the monetary policy trilemma is that a country cannot simultaneously achieve (1) a fixed exchange rate regime, (2) monetary policy independence, and (3) free capital flows. With the onset of the pandemic, the CBN’s primary source of foreign exchange earnings, oil receipts, deteriorated. Also, heightened foreign investor aversion towards EM and FM assets, coupled with the CBN’s reduced ability to defend the currency, led to FPIs reducing their exposure to naira denominated assets amid capital flow reversals. Consequently, capital inflows became depressed. In its response, the CBN maintained its hold

on the exchange rate and attained monetary policy independence to a large extent but could not achieve free capital flows - validating the policy trilemma.

To reduce the pressure on the local currency, the CBN adopted implicit capital control measures while also tacitly devaluing the naira by c.8.3% in the I&E Window by adjusting its intervention rate upwards to NGN395.00 (Year start: NGN364.79) in the year. It also devalued the naira at the official window by 23.8% to NGN379 (Year start: NGN306.00). Nigeria also received USD3.40 billion non-conditional financing from the IMF under the RFI facility, which provided some respite for the external reserves. The reserves had depleted by as much as 13.4% by the end of April. The loan, plus the CBN's capital control measures, have allowed the CBN to maintain the reserves at above USD35.00 billion since then.

Figure 52: FX Reserves (USD billion) and Exchange Rates (USD/NGN)



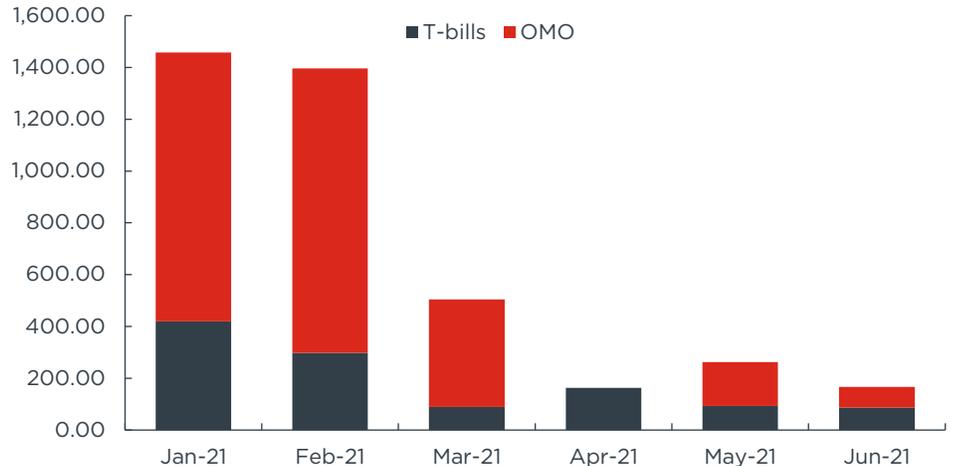
Source: CBN, Cordros Research

The MPC Will Be at A Crossroads in 2021

In 2020, the MPC emphasised that the current inflationary pressures are due to supply-side factors. Hence, tightening would not be an effective response in addressing price pressures. Although the committee's view is justifiable, anecdotal evidence suggests the exchange rate depreciation and liquidity surfeit have played a role in stoking inflationary pressures. In our opinion, the committee's somewhat cautious tone during its last meeting on the 23rd November is a pointer that inflation expectations also played a crucial role in their decision to maintain the status quo. A reduction in interest rates would have pushed real returns further into the negative territory. **We think the MPC appears to be caught at a crossroads - (1) keeping interest rates low to support economic recovery while easing government financing pressures, or (2) tightening to attract FPIs to mitigate currency pressures and restore**

stability in the external sector. The MPC’s body language suggests they are adopting a “wait and see approach” - allowing previous policy decisions to permeate the economy while keeping an eye on the oil market to see if oil prices will be sustained above USD50/bbl levels.

Figure 53: Maturity Profile (NGN billion)



Source: FMDQ, CBN, Cordros Research

Base Case: the MPC Shoots for Option 2 and Hikes Rate

Our base case expectation for 2021 is that monetary policy will remain dovish until at least Q1-21, where we expect the MPR to remain unchanged. Our view is based on our expectation that growth will remain negative until Q2-2021 and comes despite the sizeable OMO maturity profile (NGN2.55 trillion) in Q1-21. This is consistent with the committee’s forward guidance that monetary policy will remain accommodative until economic recovery gains a foothold.

As mentioned initially, we believe monetary policy tightening is inevitable from Q2-21. Hence, we expect the CBN to go for option (2) in Q2-21 and hike the MPR by 50bps with the possibility of another 50bps hike in H2-21.

Scenarios: Extent of a Rate Hike is Dependent on External Conditions

The MPC’s decision to support economic recovery will come at the expense of price and exchange rate stability. Although the MPC’s decision to maintain the status quo at the November meeting was in line with consensus expectation, the fact that it was a unanimous decision sent a signal to us that the doves have aligned swiftly into a more cautious stance. Before the November meeting, we note that six members voted to reduce the MPR by 100bps, one voted for a 50bps reduction, and three voted to hold it in the September policy meeting. For us, the rapid change in the voting pattern suggests the committee acknowledges that it

runs the risk of tightening aggressively if external conditions do not improve as expected over 2021. **In our view, the extent of tightening will largely depend on external conditions, particularly the oil market.**

Downside Case: If oil prices trade below USD50.00/bbl, we envisage a somewhat aggressive tightening as the CBN attempts to attract inflows and rebalance the external sector. The widening fiscal imbalance to be faced by the government will also require increased yields to entice domestic investors, strengthening our view. Although we think the FGN is likely to tap into the Eurobond market next year, it is unlikely to provide the much-needed support required to rebalance the external account in the medium-to-long-term. **Under this case, we expect the MPC to hike the interest rate by 200bps between Q2-21 and Q4-21, completely reversing the cuts made in 2020.**

Upside Case: where conditions in the oil market show remarkable improvement and oil prices trade well above USD50.00/bbl, we expect reduced currency pressures as the CBN will be better positioned to increase its intervention in the official windows. Notwithstanding, it would still need to attract FPIs to support the reserves. **Under this scenario, we see the MPC hiking the MPR moderately by 50bps over 2021.**

Fiscal Policy.

Proposed 2021 Budget: Conservative but Risks Abound

Nigeria's fragile fiscal position was exacerbated by the COVID-19 induced economic slowdown. A steep decline in crude oil prices and weaker prospects for non-oil revenue forced the fiscal authorities to revise the estimates for the 2020 budget in July. Over the first eight months of 2020, the budget implementation rate stood at c.94%. On the surface, this appears like good news to cheer. However, the devil is in the details, given that capital expenditure accounted for just 12% of total FGN expenditure while recurrent expenditure exceeded its budgeted amount by 1.5%. The government recorded a large revenue miss owing to shortfalls in non-oil revenue (23% below target) and independent revenue (55% below target) which resulted in a wider (+21% in 8M-20) than budgeted fiscal deficit.

For 2021FY, we expect the total retained revenue of the FGN to print NGN3.95 trillion - oil revenue of NGN2.0 trillion, non-oil revenue of NGN1.24 trillion and other revenues of NGN710.0billion. On expenditure, we expect capital expenditure of NGN1.78 trillion compared to the budgeted figure of NGN3.60 trillion. However, we expect 100.0% performance in recurrent expenditure (NGN7.41 trillion), while the statutory transfers are expected to print NGN415.20 billion. **Overall, we see the total FGN expenditure, excluding the top 10 GOEs and project tied loans, at NGN9.61 trillion. Sequentially, our base case scenario suggests a total fiscal deficit of NGN5.66 trillion (excluding GOEs and project-tied loans). If we include the GOEs and project-tied loans, our model implies that the fiscal deficit will print NGN6.37 trillion in 2021FY.**

A divergence from the norm?

The 2021 budget, prepared in line with the Medium-Term Expenditure Framework (2020 - 2023) and tagged the "Budget of Economic Recovery and Resilience," was presented to the National Assembly in early October. We note that the budget's early presentation is consistent with the government's resolve to restore the nation to an organic budget calendar year (January-December) to enhance implementation. The government proposed NGN13.08 trillion, 21.0% higher than the 2020 revised budget (NGN10.81 trillion). Simultaneously, the expected revenue was set at NGN7.89 trillion, 35.2% higher than the 2020 revised budget. The amounts translate to a 4.4% increase in the fiscal deficit to NGN5.20 trillion (2020: NGN4.98 trillion) or 3.64% of GDP (2020: 3.57%)

Conservative Revenue Targets but Risks Abound

Oil revenue is expected to increase by 98% to NGN2.01 trillion (25.5% of the total revenue), following the upward adjustments in oil price and production assumptions (including condensates) to USD40/bbl (2020: USD28/bbl) and 1.86mb/d (2020: 1.80mb/d), respectively. We highlight that the substantial increase is reflective of the low base in 2020 following the 62% cut in the initial budget estimates following the downturn in the oil market. That said, we regard the oil price assumption to be somewhat conservative, given expectations of recovery in the global economy in 2021 from the pandemic-induced downturn in 2020. **Based on our oil production estimate of 1.82mb/d in 2021, we project oil revenue of NGN2.0 trillion.**

The government also adopted a conservative stance on non-oil revenue, as it projects a decline of 8% to NGN1.49 trillion (18.5% of the total revenue), predicated on lower CIT (-17%) and VAT (-16%). The downward adjustment on CIT and VAT does not come as a surprise to us, given that the lingering impact of the pandemic, pre-existing structural barriers and subdued economic activities will likely hurt corporate profits. At the same time, persistent inflationary pressures and weak income growth will drag the latter despite the continued implementation of the increase in the VAT rate from 5% to 7.5%. Overall, we believe the performance of non-oil revenue will depend on the pattern and shape of recovery in economic activities. **Our baseline expectation is that the recovery in economic activities and improved tax administration framework will ensure a performance ratio of c.84% (2019; 85.4% and 52.8% in 2020E). Thus, we project non-oil revenue of NGN1.24 trillion.** A protracted recovery in economic activities, persistent inflationary pressures, FX liquidity challenges and insecurity in the northern region are key downside risks to non-oil revenue, in our view.

Asides from oil and non-oil revenues, the government expects to generate the sum of NGN3.7 trillion from other revenues (55.6% of the total revenue). The budget details reveal that the FGN expects to receive N961.89 billion from independent revenue, NGN677.01 billion from signature bonus & renewals, NGN500.00 billion from stamp duty, NGN387.53 billion from grants, donor funding and domestic recoveries, NGN300.00 billion from special accounts, among others. Historically, the government has grossly underperformed in generating revenue from independent sources. Weak operational efficiencies in most state-owned enterprises (SOEs) have contributed to shortfalls in the Independent Revenue amid a reluctance on the part of the government in commercialising and privatising some. Between 2015 and 2019, the average performance ratio from independent revenue stood at 50.7%. **Overall, we project**

FGN's total retained revenue to print at NGN3.95 trillion (39.6% short of budget).

Table 2: Breakdown of 2021 proposed budget (NGN trillion)

Fiscal Items	2021 (Proposed)	2020 (Revised)
Assumptions		
Oil production volume (mb/d)	1.86	1.80
Benchmark oil price (USD/bbl)	40.00	28.00
Exchange Rate (USD/NGN)	379.00	360.00
Revenue		
FGN retained revenue	6.54	5.37
Oil & related revenue	2.01	1.01
Non-oil tax revenue	1.49	1.62
Other revenue	2.83	2.64
Expenditure		
Gross FGN Expenditure	11.02	9.97
Statutory transfers	0.48	0.43
Debt service	3.12	2.68
Sinking fund	0.22	0.27
Recurrent (non-debt) expenditure	5.65	4.94
Capital expenditure (ex-transfers)	3.60	2.49
Fiscal deficit	4.49	4.61

Source: Budget Office, Cordros Research

Plugging the Deficit - From Where will the Money Come?

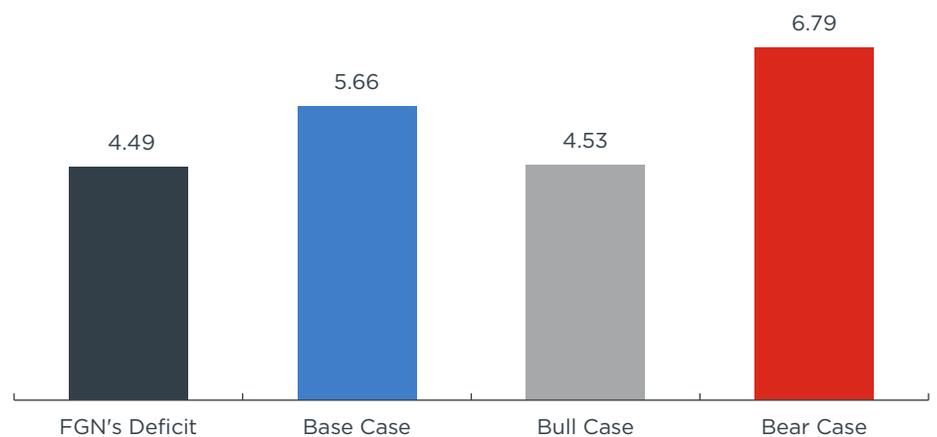
Based on the details of the budget proposal, the fiscal deficit of NGN5.20 trillion (including GOEs and project-tied loans) will be financed by borrowings (NGN4.28 trillion) split equally between domestic and foreign borrowings, multilateral/bilateral loan drawdowns (NGN709.69 billion) and privatisation proceeds (NGN205.15 billion). On foreign borrowings, considering that the government obtained non-conditional multilateral financing in 2020 from the IMF, we envisage the government is likely to make a return to the Eurobond market following two years of inactivity. Indeed, the low yields in the global market supported by the dovish chorus among systemically important central banks should engender the government to tap into the market.

The CBN's financial repression strategy ensured the government faced minimal deficit financing pressures in 2020, albeit debt sustainability metrics remain weak, with debt service to revenue ratio spiking to an all-time high of 99.2% in Q1-20. At the start of the year, the DMO leveraged the low yield environment and strong demand for government securities to frontload domestic issuances. Based on data from the DMO, net issuance of (Bonds & T-Bills) over the first eight months of 2020 stood at NGN1.65 trillion. On an annualised basis, the domestic borrowing

was c.61% above the total net issuance of (Bonds & T-Bills) N1.54 trillion in 2019 from the local debt market.

Over the first half of 2021, we believe the domestic market presents the federal government with an opportunity to frontload domestic issuances without triggering upward repricing of yields. We expect the dovish monetary bias of the apex bank to keep system liquidity robust. However, we think there is a high possibility of an upward market repricing of interest rates in H2-20 if revenue challenges become amplified by a prolonged recovery in the oil market and faltering growth momentum, prompting the government to be aggressive with domestic issuances.

Figure 54: Estimated Budget Deficit Range excluding top 10 GOEs (NGN' trillion)



Source: Budget Office, Cordros Research estimates

On debt sustainability, we note that the nation's debt burden has come under increased scrutiny in recent times, given the substantial increase in public debt amid underperformance in revenue targets. For context, public debt has more than doubled to N27.40 trillion in 2019 from the pre-recession level of NGN12.60 trillion in 2015. The FGN's retained revenue grew by just 27.2% to N4.12 trillion in 2019 from the pre-recession level of NGN3.24 trillion in 2015. Though the debt-to-GDP ratio of 19% (2019FY) remains within the acceptable threshold, the deterioration in debt/service cost to c. 63.0% in 2019 (2015: c. 38.0%) is a concern.

Without downplaying the importance of an expansionary fiscal policy under current economic conditions, we note that a high proportion of tax revenue absorbed by debt servicing will limit available public resources for investment in capital formation, including social spending needs. Ultimately, the government is faced with the difficult task of balancing borrowings to support near-term growth and avoiding a further buildup of debt that will further weaken debt sustainability

metrics. This is more so that actual output will likely lag potential output over the medium term.

Figure 55: Debt Service to Revenue Ratio

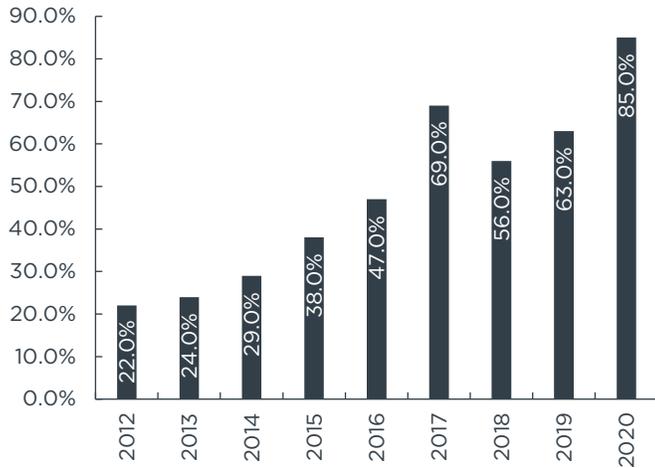
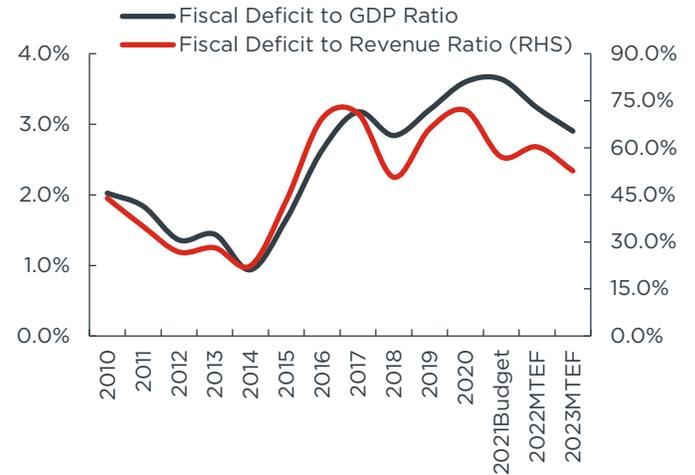


Figure 56: Fiscal Deficit to GDP Ratio



Source: Budget Office, CBN, Cordros Research

Financial Markets.

Fixed Income.

A Monumental Year Points to Caution Ahead

As impressive a year as 2020 was for other asset classes, the performance of the fixed income market outstripped that of all traditional asset classes, as a combination of market dynamics and policy actions resulted in yields paring to record low levels. Consequently, investors recorded impressive returns even as the pandemic left performance across other asset classes pressured for a large part of the year, before a recovery in the latter part of the year.

In 2021, we expect a general reversal. This expectation of a turnaround in yields should result in market volumes paring markedly, as investors thread the part of caution. Nonetheless, we expect yields to remain in the low single-digit region through the first half of 2021, as economic managers prioritise growth over price stability. However, given the weak macroeconomic backdrop, which points towards significant exchange rate pressure, and the likely change of imperative as the world moves into a post-pandemic era, we expect a shift in focus towards the overarching objective of ensuring price stability. This shift in focus will result in policy-driven action to attract investors and incentivise investments in naira assets.

2020 in Review

At the start of 2020, having assessed the confluence of ex- and endogenous factors, we were of the view that the fixed income market would be a volatile one in the year, and that on a balance of factors, yields would most likely trend downwards.

Consequently, fixed income was the best performing traditional asset class, due to a combination of (1) favourable market dynamics, and (2) a switch to a more accommodative policy stance from the monetary and fiscal authorities. Overall, the preceding led to yields declining to record low levels across all instruments in the market.

On yields, Nigerian Treasury Bills (NTBs) yields trended to near-zero levels, as the segregation of the market led to a significant imbalance between demand and supply. Interestingly, the story was a similar in the OMO secondary market, in which deposit money banks are the major players – primary market yields on OMO bills contracted by 923bps in the year to 4.1% as of December 17 2020. Similarly, the contraction in yields in the bonds market was quite significant, declining by an average of 554bps to 5.2%.

Figure 57: Market Yields 2020 (%)

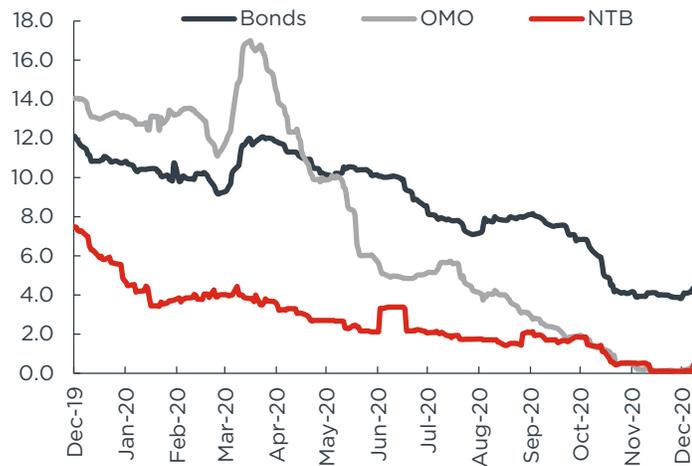
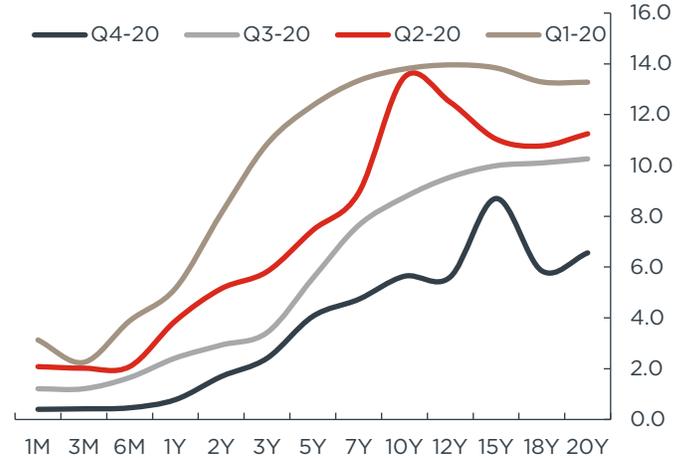


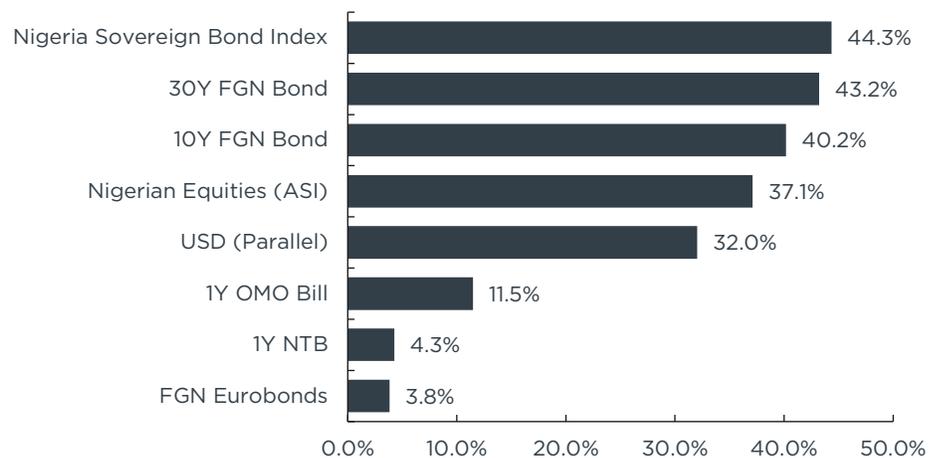
Figure 58: Quarterly Yield Curve 2020 (%)



Source: FMDQ, Cordros Research

While we had expected that significant liquidity from maturing OMO bills in 2020 would pressure market yields downwards, we did not foresee deliberate monetary and fiscal action to bring yields to record low levels. We held this view, even though a switch to an accommodative policy stance from the monetary authority was inevitable as the pandemic swept through the globe causing economies to issue shelter-in-place orders which were crippling for growth across regions.

Figure 59: Asset Classes Performance 2020 (%)



Source: NSE, FMDQ, AbokiFX, Cordros Research | As of 17.12.20

Outlook: Market Will Retrace in 2021

We believe that the performance in the fixed income market will be a tale of two halves. We expect yields to remain in the low single-digit territory through H1-21, with a moderate uptrend to account for reduced market participation as investors

seek yields in other asset classes. However, in the latter part of the year, we believe that a combination of (1) weak market participation, (2) revision of monetary policy to a tightening cycle, (3) widening fiscal deficit, and (4) fragile macroeconomic environment will lead to an increase in yields over 2021.

Domestic Participation Will Remain Strong but Wither in Comparison

The dynamics of the market in 2020 supported strong domestic participation, primarily due to the significant liquidity profile in the year, mostly belonging to pension fund managers who are precluded from investing in foreign-denominated assets.

Given that these maturities expired in 2020, this same scenario may not be expected to play out in 2021, even though asset maturities and coupons worth NGN5.50 trillion and NGN1.35 trillion respectively, are expected in the year.

With the market now without the significant maturity profile from the liquidity management instruments, there will be less demand pressure relative to supply. Also, with the projected deficit from the 2021 budget (Cordros' base case estimate: NGN5.66 trillion; NGN1.17 trillion above the estimate in the proposed budget), it seems that the market will be oversupplied. However, our view for yields from this perspective is tempered by the fact that the federal government remains the oversized issuer in the market. This will allow for a great deal of influence over yields as has been the case in 2020.

That being said, the substandard level of yields relative to inflation, which is only expected to widen in the coming year, will dampen domestic participation. Also, given this dynamic and the expectation that a tighter monetary policy stance will be required later in 2021, investors are wary of accruing losses, from what is likely going to be a swift change in policy direction.

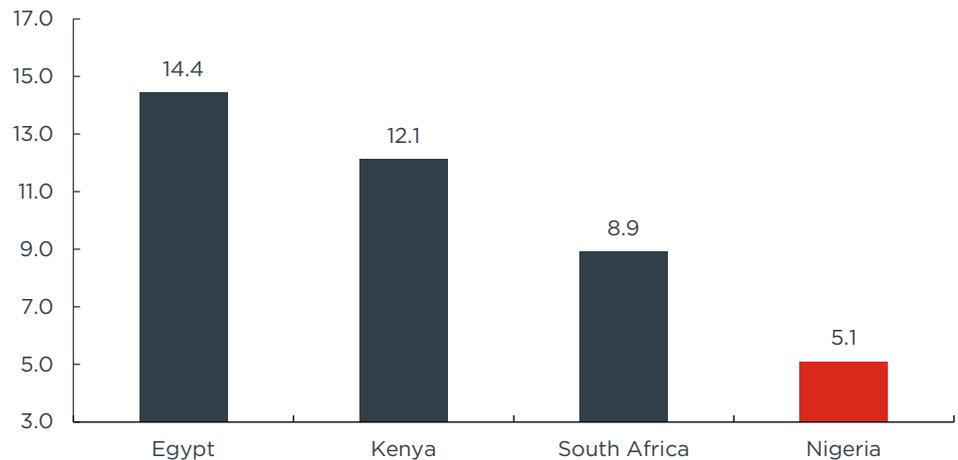
Global Capital Flows May Bypass Nigeria

The low level of global interest rates should ordinarily have been a boon for the Nigerian fixed income market, as a break from savings to investment-led growth post-COVID-19 changes global flow dynamics. In this scenario, the beneficiaries of this change in dynamic would be emerging and frontier market economies with strong macroeconomic fundamentals, good democratic standards, and strong institutions.

Also, given (1) the current yield environment in the country relative to peer countries, (2) policy flip-flops by economic managers, and (3) a distinct lack of forward guidance from same, Nigeria is likely to be bypassed. This view, further

contextualised by substantial capital repatriation that we expect in 2021 as the currency market opens up, signals market pressure in 2021.

Figure 60: Fixed Income Yields of Peer Countries 2020 YE (%)



Source: Bloomberg, Cordros Research

All Signs Pointing Northwards

Given the balance of factors that we believe will affect the market over 2021, we believe the probability is tilted towards the upside. Nonetheless, we expect the market to trend downwards in H1-21 as the monetary and fiscal authorities push 'lower-for-longer' yields with the purpose of (1) pursuing a growth mandate to support post-pandemic recovery, and (2) managing the debt burden of the federal government. However, as issues concerning price levels come to the forefront, we expect policy action to drive foreign portfolio inflows into the country.

Consequently, we expect yields the average yields on bonds to trend upwards to c.7.0%, while yields on NTB instruments trend to c.1.0%. The reason for this disparity is rooted in the demand and supply dynamics between the two markets. The instruments on offer in the Treasury bills market are limited relative to buyers (especially given regulatory requirements), even with a larger frequency of issuances. This should result in market participants' demand pressuring yields on shorter-dated instruments.

Below Expectations: Nonetheless, we apportion a probability to yields being tethered to the low single-digit region through most of 2021, provided that there isn't widespread adoption of the COVID-19 vaccine, and the situation in the country becomes dire; with increasing cases of infections and deaths. In this scenario, there would be reduced pressure on the reserves due to a likely cessation of travel and weaker levels of imports, amongst others. This would

essentially allow the prolonging of the inevitable and result in yields remaining tethered to the lower single-digit region. That being said, we do not believe there is a significant downside for yields from this point. We only see a marginal decline from these levels on significantly weaker demand in 2021. Our view is predicated upon investment managers focusing investments on assets with the potential of generating positive inflation-adjusted returns.

Above Expectations: The country's balance of payments position deteriorates further from this point, leading to significant pressure on the currency. This would require FPIs to remain weak, just as the price of crude oil remains weak or deteriorates, leading to a precipitous decline in reserves and the CBN's ability to defend the currency. In this scenario, we expect yields to trend upwards on fixed income instruments precipitously, as the monetary authority would try to attract investors.

Equities.

Feeling the Quality with Equities

This has been a truly exceptional year in, and outside of financial markets. Nigerian equities sank to 8-year lows, as investors fled to safety due the pandemic, but also saw a rapid recovery to 2-year highs as the hunt for yield intensified.

We expect it to be a tale of two halves for Nigerian equities in 2021, with the market delivering further upside in the first half of 2021 before retracing slightly in the second half on an expected reversal in fixed income yields. The sources of risks remain as the macro story remains uninspiring, and valuations are elevated. However, we are of the view that the mix of (1) elevated liquidity, (2) low interest rates, (3) attractive dividend yields, and (4) earnings recovery, point to a large probability of an extended bull market into 2021.

2020 in Review

We witnessed historically volatile markets and the fastest equities crash since the 2008/2009 crisis. The combination of expansionary monetary and fiscal policy stances helped mitigate the initial shock of the pandemic, and the consequent liquidity surfeit led to a strong market rebound. At the time of writing, year-to-date the All-Share Index has returned 32.2% (December 17 2020), and Nigerian stocks are among the best performing globally.

Figure 61: NSE ASI performance in 2020 (points)

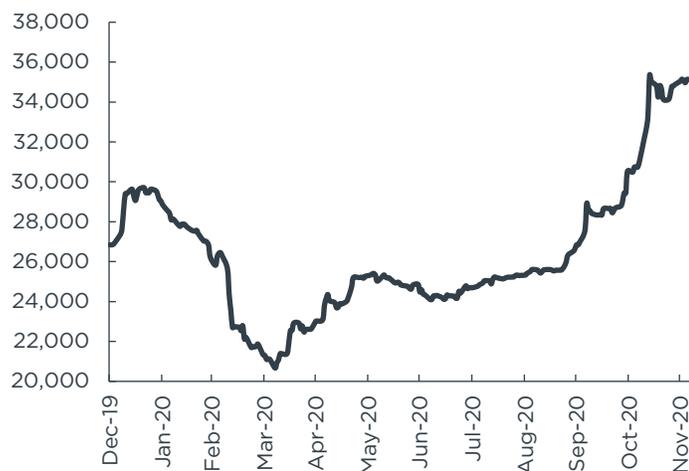


Figure 62: Return: Nigerian vs frontier and global equities in 2020



Source: NSE, Bloomberg, Cordros Research

At the start of the year, we stated that fundamentals were not strong enough to drive a natural correction in the equities market but that the CBN's policy directives, which caused fixed income yields to decline precipitously, would offer

some respite to the domestic bourse. This played out in January as the opportunity for a dividend yield investment strategy presented itself. However, this could not be sustained over the rest of Q1 on (1) weak foreign participation in the market due to weak macro fundamentals and fears concerning a possible devaluation, (2) weak domestic participation, and (3) the outbreak of the COVID-19 virus.

Since hitting an 8-year low in April, the market unexpectedly rebounded strongly by 71.7%, at the time of writing. The deliberate actions by the fiscal and monetary authorities to drive interest rates down significantly were the primary drivers of the gains. Local investors, who had over NGN5.0 trillion in OMO maturities to deploy, were left with no choice but to chase positive real returns in the equities market. Following the Q1 selloffs, the equities market provided a massive opportunity for bargain hunting with many stocks trading at huge discounts and offering higher dividend yields than fixed income. Notably, yields on fixed income instruments became technically un-investible – short term treasuries traded at sub-1% levels while long tenor bonds traded below 7%.

On fund flows, domestic investors had brought in NGN159.81 billion into the equities market as of September 2020, compared to NGN94.03 billion over the whole of 2019. Conversely, foreign investors exited the market en-masse as FX illiquidity issues persisted. Data from the NSE showed that flows from foreign investors were negative in all months of 2020, save for May, when trapped investors re-invested dividends. Overall, foreign investor net outflows have totalled NGN159.62 billion YTD, a record high, with participation, compared to domestic investors falling to a record low.

Figure 63: NSE Investor flows (NGN billion)

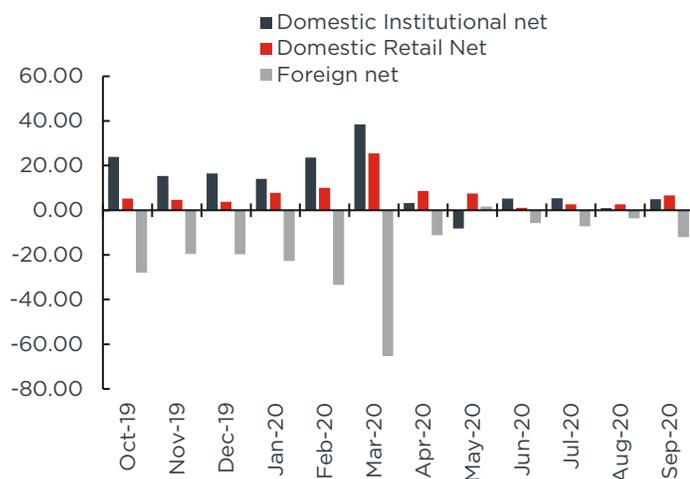
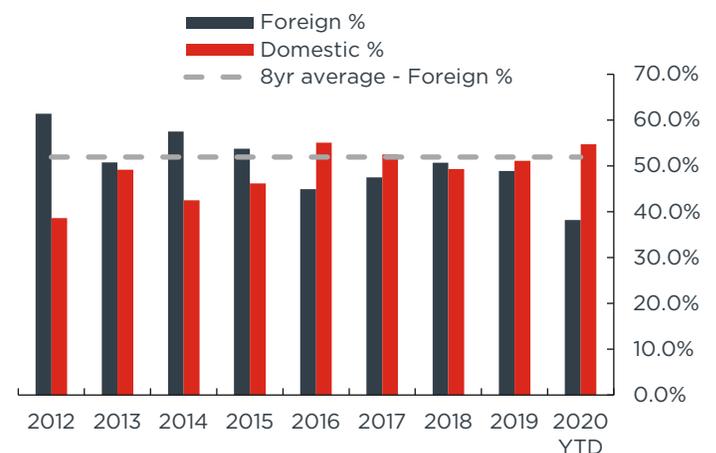


Figure 64: Foreign vs Domestic Participation in the NSE



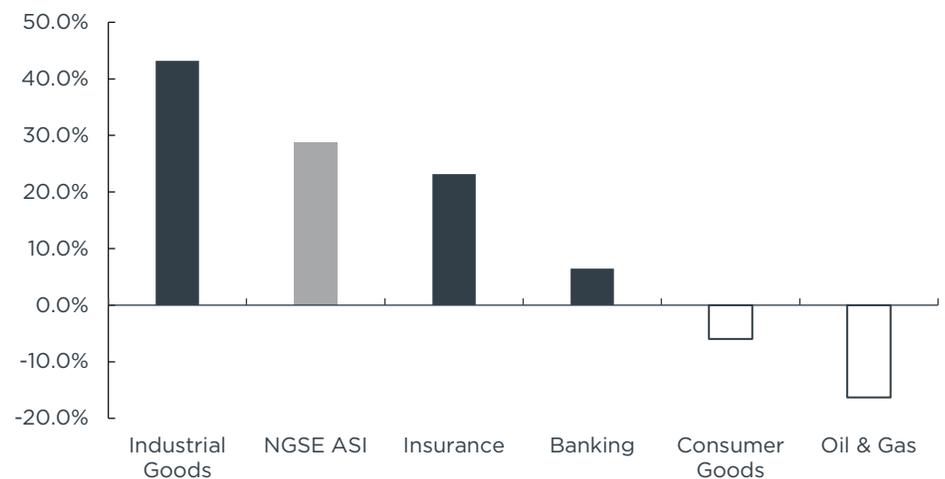
Source: NSE, Cordros Research, 30.09.2020

Where Did Investors Play?

The gains this year were led by what we tagged the “best COVID-19 defensives”, the Telco stocks. Local investors piled into MTNN (+47.6%), whose earnings were resilient and provided a significant price upside. In comparison, foreign investors flocked to the dual-listed AIRTELAFRI (+135.5%) as an alternative means to repatriate funds.

Industrial Goods (+50.4%) stocks, mainly the big three Cement firms – DANGCEM (+37.3%), BUACEMENT (+43.0%), and WAPCO (+43.8%) – also lent a hand. Investors increasingly opted for these “cyclical” companies – whose earnings growth are tied to the economic performance – and those whose earnings performed better than initially expected as the government eased lockdown measures.

Figure 65: Sector Index Returns vs ASI



Source: NSE, Cordros Research

Investors also looked to the Banking (+8.3%) stocks, particularly GUARANTY (+28.3%) and ZENITHBANK (+50.4%), as they offered best-in-class dividend yields and recorded better than expected earnings despite the effects of the pandemic.

Oil & Gas stocks (-16.0%) declined on average, driven by sector heavyweight SEPLAT (-33.3%), whose earnings suffered from the oil price crash. However, reforms in the downstream subsector offered a boost to oil marketers’ stocks – MOBIL (+61.0%) and TOTAL (+25.4%) both surged in the year as the removal of the PMS retail price cap allowed the companies to enjoy margin expansions.

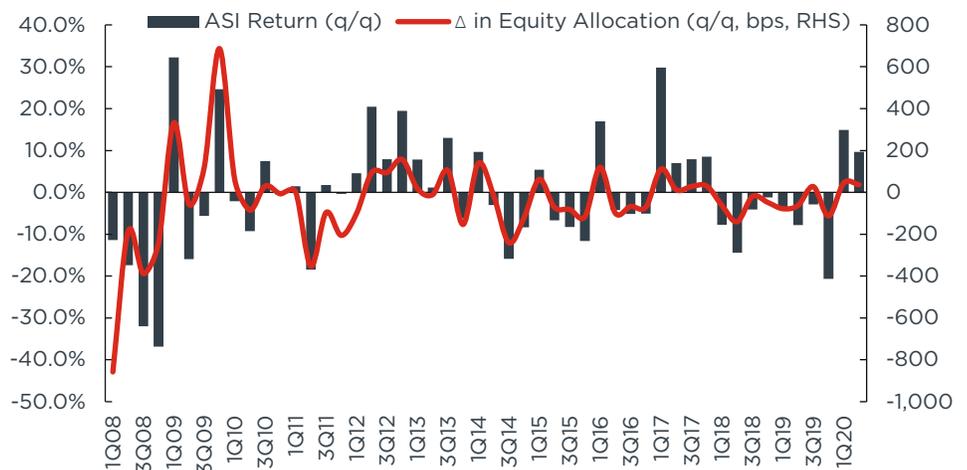
Outlook: Equities to Still Drive Returns In 2021

Similar to our outlook for fixed income, we expect it to be a tale of two halves for Nigerian equities in 2021, with the market delivering further upside in the first half of 2021 before retracing slightly in the second half on an expected reversal in fixed income yields. The sources of risks remain plenty, the macro story remains uninspiring, and valuations are elevated. However, we think the mix of (1) elevated liquidity, (2) low interest rates, (3) attractive dividend yields, and (4) recovery in earnings argues in favour of an extension of the equity bull market into 2021.

Market performance in H1-2021 will be primarily determined by domestic participation which will be supported by the expected liquidity surfeit and the resultant low FI yield environment. Additionally, investors positioning for 2020FY dividends in Q1-21 should see increased buying activity in the market. Foreign investors, on the other hand, will stay away from the market as long as FX illiquidity issues persist.

As we highlighted in our outlook for Monetary Policy, we expect the monetary authorities to begin a tightening cycle in H2-2021, which will signal higher fixed income yields. Consequently, domestic investor activity is likely to weaken substantially. We note that equity market returns and changes in PFAs asset allocation to equities are strongly correlated (Figure 6). Therefore, in the absence of foreign investor support, equity markets will decline as PFAs reduce their exposure, hoping the expected yield retracement will be prolonged. Domestic retail investors will most likely follow suit. As a result, gains from H1-20 are likely to be eroded.

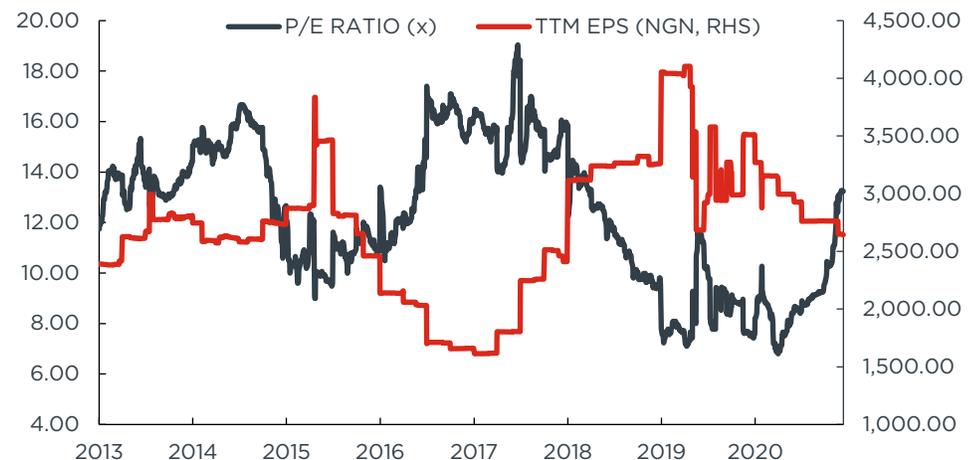
Figure 66: Pension Allocation to Equities vs ASI Returns



Source: NSE, CBN, Bloomberg, Cordros Research

In bubble territory?: With the COVID-19 pandemic triggering a collapse in earnings, the markets relied on multiple expansion to rebound. Unprecedented low rates in the market and increased liquidity helped drive the expansion of multiples and equity returns. The All-Share Index is currently trading above 13x earnings, well above its pre-Covid-19 crisis level of 9x, and par with levels reached during the last domestic investor driven rally in H1-2016. This multiple also appears slightly elevated from a longer-term perspective (7-year average: 12.2x).

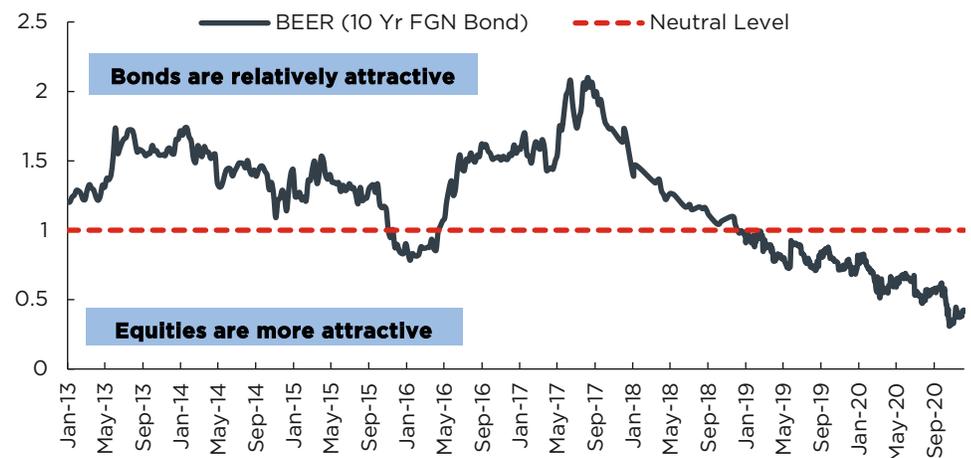
Figure 67: NSE ASI - Price-to-Earnings Ratio and Earnings



Source: Bloomberg, Cordros Research

It's all relative: Indeed, while valuations remain slightly higher than their historical average, they appear fair when taking into account the level of interest rates. At 691 basis points, the spread between the earnings yield and the 10-year risk-free rate is at records highs. For further comparison, we looked at the Bond Equity Earnings-yield Ratio (BEER). The BEER is a metric that investors often use to evaluate the relationship between earnings yield of a stock market (the inverse of the price-to-earnings ratio) relative to bonds. A number above one indicates that bonds offer more value than equities (Figure 8). The metric shows that for domestic investors, there is more value in equities, compared to bonds, than has been in at least the last seven years.

Figure 68: Bond Equity Earnings Yield Ratio



Source: NSE, FMDQ, Bloomberg, Cordros Research

Overall, we think this disconnect between the strong equities and the weak economy could persist. Low rates are likely to continue to provide some valuation support for equities, and more cyclical parts of the market can catch up with the strong performance of defensive stocks as the economy recovers.

Dividends to help: Without re-rating, earnings growth and shareholder income should primarily drive equity returns. On the latter, after a slowdown in recent months, companies are likely to return to rewarding shareholders next year in the form of higher dividends. While it may take a couple of years to recover to pre-pandemic levels fully, 2021 is likely to be a much more supportive environment for income investors. However, with a long road to recovery ahead, we believe that the focus should be on the sustainability of dividends rather than their absolute levels.

Earnings to rebound strongly: Consensus expectation is that Nigerian equities will deliver c.27.0% y/y earnings growth in 2021, leaving earnings per share 3.0% above 2019 levels. While this may seem optimistic, this year highlighted that many companies can quickly adapt to a challenging environment. Should a vaccine be widely available, and the government continue to support the economy, we would not be surprised to see 2021 earnings coming close to match those seen last year. However, we can expect wide discrepancies in the pace of the recovery at the sector and stock level.

Market Return Scenarios

	Base Case	Bear Case	Bull Case
Market Return	+12.8%	-21.8%	+27.2%
ASI Level	38,633.96	26,788.97	43,565.90
Probability	50.0%	35.0%	15.0%

Source: Cordros Research estimates

Key factors to watch – (a) downside risks: (1) reversal in FI yield direction, (2) significantly lower earnings and dividend payouts, (3) surge in COVID cases, (4) further decline oil prices

Key factors to watch – (b) upside risks: (1) sustained period of higher oil prices and increased FX liquidity, (2) devaluation of the naira, (3) negative FI yields, (4) better than expected earnings, (5) widespread adoption of COVID vaccine in Nigeria.

Sectors

Banks

Resilient Despite the Pandemic: While the economic impact of the pandemic has been much less than during the 2008/2009 financial crisis, banks still had a lot to do as shelter-in-place orders forced revisions of operating models. And it is worthy to note that, despite the challenging economic and regulatory environments, the transition to mostly remote working operations was as seamless as may be expected given the timeframe under which it was required. In general, customers have been served, employees have been productive, and profitability has not deteriorated markedly. *References to sector performance refer to the 12 banks listed on the Nigerian Stock Exchange unless otherwise stated.*

FY-20 was Always Going to be a Difficult One: Regardless of the pandemic, 2020 was always going to be a challenging one for banks. The Loans-to-Funding ratio (LFR) directive of 2019, combined with the cash reserve ratio (CRR), already left banks with little room to manoeuvre. However, further indiscriminate CRR debits which had already become a hallmark of 2019 despite institution only at the tail end of the year, pressured liquidity for banks in 2020. Specifically, the actions exerted downward pressure on industry net interest margin (given CRR is held zero interest) – sector NIM as of 9M-20 was 6.7% relative to FY-19: 7.0%.

LFR Directive Sparks Growth; Pandemic Causes Pullback: While the growth outlook should ordinarily have been towards diminished loan growth and payment transaction volumes. On the former, risk asset creation has increased given the initial aggressive move towards alignment with the new statutory LFR limit – credit to the private sector grew by 22.3% y/y and 15.6% YTD, according to data compiled by the NBS for the wider sector. However, risks to risk asset creation became elevated as the pandemic ravaged across the globe, and the country then implemented a lockdown.

Financial Performance Reflects Resiliency: Despite what should have ordinarily been a tough year for the banks, the average return on equity (ROE) only moderately pared to 14.1% as of 9M-20 (FY-19: 15.2%). When compared to the performance of peer African nations (South Africa: 13.1% and Ghana: 13.5%), it denotes the resilience of the sector. This performance was supported by substantial loan growth– which supported interest income growth despite record low fixed-income yields–, a realignment of currency (19.5% realignment/depreciation on CBN official rate to NGN379.00/USD), trading revenue, and tight cost efficiency (9M-20: 64.0%; FY-19: 65.9%). All of these supported a generally stable financial performance, as gross earnings expanded by 0.1% y/y, while PBT declined by 6.1% y/y.

Liquidity Positions Pressured by Persistent CRR Debits: The consistent and sizeable CRR debits undoubtedly exerted pressure on banks' liquidity positions. As may be expected, this impacted the ability of the banks to grow their risk asset portfolios measurably and perform their intermediation role even if they wanted to and affected monetary policy actions to see the country through the pandemic. Acknowledging the mismatch between actions and the aim of the policy, the CBN announced a Special Bill would be issued to banks to improve the liquidity positions and by extension result in continued growth in credit to the private sector. The apex authority eventually issued instruments worth NGN4.20 trillion (81-day tenor) on December 10 2020.

Forbearance Deflects Pandemic-induced Asset Quality Deterioration: Given regulatory forbearance to not reclassify distressed restructures, the primary asset quality macro-prudential ratio doesn't reflect the economic damage of the pandemic – non-performing loans settled at 6.0% as of 9M-20, representing a moderate deterioration of 0.47 ppts YTD. While this is partly due to the significant expansion in sector credit risk exposure, forbearance has also played a part in this outcome.

The level of provisioning, however, is more reflective, as credit impairment charges across the sector have risen by 77.5% y/y, representing 0.7% of industry loans (FY-19: 0.5%). Contextualised by the significant growth in credit in the period, the impact of the pandemic on asset quality becomes clearer.

We are 'Overweight' the sector: Banking sector stocks have performed well during 2020, using the NSE's Banking-10 index as a proxy (+11.9% YTD return as of December 18 2020). However, this standalone view doesn't tell the story of what has been a tumultuous year that culminated in a strong recovery in value for these stocks in H2-20. Market participants returned to equities en-masse as yields on fixed-income instruments declined precipitously. We expect this will remain the theme for the market until yields on Treasury instruments rise once more. Overall, we expect a combination of (1) strong dividend yield expectations, and (2) resiliency of sector players into the FY-21 financial period to support price performances.

That being said, our outlook is cautious. Firstly, the macroeconomic outlook for the country, while relatively positive after the damage of 2020, remains fraught with headwinds, which will leave the market risk above average. Hence, measurable intermediation, while maintaining strong asset quality, will be an arduous task. Secondly, rates on fixed-income securities are expected to remain low through H1-21. This will pressure interest margins (NIMs) and create strong headwinds to funded income growth. Finally, the confluence of the factors stated, as well as a lack of meaningful revision to the application of regulator rules, will force banks to find new pathways to profitable growth away from the traditional sources of income; early movers will have the advantage.

Cement

Pandemic Wreaks Havoc on Construction Activities: Following a decent start to the year wherein cement sector GDP grew by 1.67% in Q1-20, the imposition of lockdown measures dampened activities in Q2-20 as construction companies, and unskilled workers had to comply with shelter-in-place orders. Suspension of activities on major construction sites and increased government focus on the healthcare sector left a negative imprint on the construction industry and by extension, demand for cement. Specifically, cement sector GDP declined by 5.54% in Q2-20, reflective of the sharp deceleration in real estate sector (-21.9% | Q1-20: -4.8%) and construction sector (-31.8% | Q1-20: +1.7%) GDPs. Besides from the pandemic-induced slowdown, we believe (1) subdued demand for residential properties partly due to shrinking real incomes, (2) the higher cost of building materials due to devaluation of the local currency, and (3) the reduced availability

of building materials due to supply chain disruptions also contributed to the weakness in the real estate sector.

Relaxation of Lockdown Measures Underpins Robust Recovery in Q3: The easing of social distancing measures in early May which lasted till the end of Q3-20 enabled the restart of construction projects previously abandoned. The easing, in conjunction with the more robust recovery in private sector demand, amid low rainfall, provided the catalyst for a strong rebound in the cement sector in Q3-20 (+12.0%). Notably, demand for new orders, according to the CBN's PMI data, averaged 61.1 points in Q3-20, an improvement from 51.8 points in Q2-20. The recovery in the sector was evident in the strong revenue growth recorded by industry players – DANGCEM (+45.5% y/y), WAPCO (+31.4% y/y) and BUACEMENT (+39.7% y/y) – in Q3. Based on our discussions with the management of our coverage names, the private sector drove the robust demand in Q3. According to Nigeria's finance minister, over the first eight months of 2020, a total of about NGN761.8 billion was released for capital projects. The amount translates to a budget performance ratio of 45.9%.

Higher FCY Denominated Costs Pressure Margins: Our coverage companies faced input cost pressures from the impact of the naira devaluation on FCY costs, particularly energy. In Q3-20, DANGCEM's energy costs surged by 25.2% y/y, almost double the increase in Q2-20 (+13.4% y/y). For Lafarge, gross margin declined to 36.9% (Q3-19: 42.0%) in Q3-20 due to the rise in the variable cost component (+61.2% y/y) of COGS. Management attributed this to higher naira equivalent costs on USD denominated cost items, namely gas contracts, spare parts and strategic raw materials.

Frail Macro Conditions to Cap Volume Growth in 2021: Volume growth in 2021e will be modest due to the lingering impact of the pandemic on government finances and household income. Subdued macro conditions will likely constrain demand for residential properties, hinder private investment in gross fixed capital formation amid legacy challenges in the real estate sector. However, we are slightly optimistic about government CAPEX spending, particularly in H1-21. Our view is underpinned by our expectation for a sustained low yield environment which would ease deficit financing pressures. The 2021 budget submitted to the National assembly showed that the government plans to spend NGN3.60trn on capital projects, an increase of 45% from the revised capital expenditure for 2020 (NGN2.49trn). The recent establishment of an infrastructure company by the FGN, which will be funded mainly by the CBN and NSIA, also lends credence to our optimism. **Overall, we forecast volume growth of 5.1% y/y and 2.1% y/y for Dangote Cement and Lafarge, respectively.** Accordingly, we expect overall

sales volume for our coverage names to grow sales by 4.4% in 2021E compared to our 2020E growth of 13.2%.

Marginal Price Increases may be Inevitable: Although the stiff competitive landscape coupled with soft industry conditions will deter industry players from raising prices substantially, we still see scope for marginal increases in prices. Our view is hinged on higher input costs associated with dollar-linked cost items which would prompt a marginal price increase to preserve margins. Based on our estimates, the price per tonne for DANGCEM rose by 3.8% y/y as at 9M-20. In our view, a critical risk to margins for industry players is the weak currency outlook. We believe a further devaluation will exert downward pressure on margins as industry players may be unable to pass on the full cost to consumers in the form of higher prices. **Overall, we forecast the ex-factory price will increase by an average of 2.2% y/y in 2021E.**

Real Estate to Recover Marginally but Will Remain in the Woods: Since the last recession of 2016/17, the real estate sector is yet to show any signs of recovery. Before Q2-20, when the industry suffered its worst negative performance on record (-21.9%), the industry recorded just one quarter of positive growth (Q1-19: +0.9%) since Q1-16. In our view, the lacklustre performance of the sector is primarily tied to Nigeria's shrinking per capita income which has undermined the demand for capital goods, especially residential properties. Over 2021, we do not think there will be a significant improvement in the demand for durable goods, particularly from the low-and-middle-income earners. Our view is hinged on our expectation of continued pressure on household incomes due to elevated inflation a higher cost of living. The residential sector will continue to struggle as long as GDP growth remains below population growth and unemployment remains high.

That said, we think the growing demand for rented apartments, among the low-and-middle-income earners, would stimulate the demand for rented residential properties. Additionally, we believe the reduction in the cost of credit, triggered by CBN's unorthodox policies (which have also impacted mortgage costs positively), may encourage the development of commercial properties. We also believe the cheaper credit will spur demand from the upper echelons of middle-class consumers who currently opt for expensive rental payments. Overall, we believe the demand for residential and commercial real estate will be affected by sub-optimal growth in GDP and infrastructure bottlenecks amidst the rising cost of building materials. In all, we expect the real estate sector to show a marginal improvement in 2021. However, the pace of recovery will be insufficient in taking growth to back into positive territory.

Excess Capacity Portends Long Term Upside for Growth: Nigeria's cement industry has experienced significant growth over the years, transforming from import-dependent to self-sufficiency and currently poised to become a hub for cement exports on the continent. Despite the significant investments made by industry players in expanding their plants, demand still dwarfs industry capacity and, as a result, has led to excess capacity. As at Q3-20, total installed production capacity, based on data from the top 3 industry players, stood at 47.9MMT, which is far above Nigeria's estimated consumption of c. 23.5MMT for 2019. Meanwhile, industry capacity is set to rise further from 47.9MMT to 50.9MMT, given BUACEMENT's proposed commissioning of its new USD450 million 3MMT Sokoto line 11 plant scheduled to come on stream in Q2-21. Accordingly, BUACEMENT's capacity will increase to 11MMT, from 8MMT currently, and may displace WAPCO as the second-largest cement producer by capacity (assuming the latter does not increase its capacity). Currently, DANGCEM ranks top of the market share charts with a share of 61.1% (installed capacity: 29.3MMT). WAPCO accounts for 21.9% (10.5MMT) of the market, while BUACEMENT has a 16.7% (8.0MMT) share of the market. Despite the opportunities presented by the enormous infrastructure and housing deficits, we expect excess capacity to remain in the short-to-medium term as demand remains constrained by tepid infrastructural spending by the government and private sector investment in capital formation. Nonetheless, we think it presents opportunities for faster growth over the medium-to-long term.

Consumer Staples

Agriculture

CPO price resilient despite the pandemic: The year 2020 was generally tepid for commodities, as the black swan occurrence of the COVID-19 pandemic, and the associated restriction of economic activities subdued demand for products across the globe. Against the preceding, the price of crude palm oil (CPO) plunged in the early months of the year, following the disruption in market dynamics. Also, global rubber prices were not spared from the rout, following an estimated 5.0% drop in rubber production, as imports from the top two rubber consumers – China and India – slowed markedly.

However, CPO price rallied in June, due to (1) supply disruptions from Indonesia and Malaysia (which make up 85% of total product supply), following the reeling effects of drought and fertiliser application in 2019, (2) the shortage of workers to man production; (3) product re-stocking by key importing countries, e.g. China, (4) the decline in the supply of other edible oils; and (5) the switch by biodiesel producers to vegetable oils for feedstock, which also boosted demand for CPO.

Despite the lockdowns, the revenue growth of major Nigerian agriculture companies - OKOMUOIL (9M-20: +23.5% y/y) and PRESCO (9M-20: +24.5% y/y) - has been impressive. The topline growth was on the back of the improved domestic price of refined palm oil compared to the previous year, and as the companies were able to push out more volumes. The aforementioned further highlights the positive impacts of the closure of the Nigerian border on CPO producers, which we discussed in our 2020 Agriculture sector outlook - See report: [Surging Volumes to Lift Earnings; All Eyes on the Border](#).

Lower prices on potential border reopening: Going into 2021, we expect CPO prices to remain high, especially in the first half of the year, and higher rubber price, especially towards the second half of the year. **The World Bank estimates CPO price at USD723.00/mt and rubber at USD1.68/kg.**

On CPO, the price forecast is primarily hinged on expected tight supply from heavyweights, Indonesia and Malaysia, as labour constraints and ageing palm tree profiles impact fresh fruit bunches (FFB) yields. Also, the effects of the La Nina weather pattern will subdue global supply in the first quarter of 2021, following the disruptive impact on CPO producing countries in Southeast Asia. Furthermore, we expect CPO prices to be supported by increased demand for vegetable oils, due to a tighter supply of soft oils such as soybean and sunflower oils.

For rubber, we expect the demand from the health sector, which soared in 2020 to remain sizeable in 2021, thus limiting the effects of reduced uptake from the auto industry as a result of declined global car sales.

On the domestic front, we highlight the potential reopening of the land borders in the first quarter of 2021, as a significant headwind for Nigerian CPO planters. The current nonexistence of an anti-smuggling deal with neighbouring West African governments exacerbates the downsides for local manufacturers. For clarity, with the borders reopened, there will be an increased supply of products in the domestic market, which mean higher competition and price erosion for local players OKOMUOIL and PRESCO.

On the back of the preceding, we forecast revenue growth of 1.2% and 3.8% for OKOMUOIL and PRESCO respectively, as we expect continued CPO volume deluge to support revenue in the year. Also, with global supply expected to be tight in 2021 amid increased demand, we expect CPO and rubber (for OKOMUOIL) exports to grow in 2021, and support revenue outturn for the year. We expect the government's "pro-agriculture" stance to continue to support the operations for both companies.

Agriculture stocks have re-rated over the last few months following the broader market rally. As a result, current valuations look stretched. At current prices, we rate OKOMUOIL (TP: NGN84.47) and PRESCO (TP: NGN63.84) a HOLD and a SELL, respectively.

Brewers

Pandemic Pressure: Brewers were significantly impacted by the lockdown in Q2 as on-trade (bars, clubs hotels) volume sales, which account for c.67% of beer sales, suffered a steep decline. Our analysis of the Big 3 brewers showed that net revenue declined by a cumulative 32.1% y/y in Q2, the worst quarterly decline on record. Noteworthy, however, was the strong recovery in topline Q3-20 (+21.8% y/y) as lockdown measures were eased. The recovery was driven by the resilient volume performance of the premium segment, which includes premium lager (NB & INTBREW) and spirits (GUINNESS). Despite the topline hit, surging inflation and FX illiquidity negatively impacted input and operating costs and as a result, margins deteriorated.

One Step Forward, Two Steps Back: With the pandemic bringing about Nigeria's second recession in 4 years, the coming year is expected to be characterised by an even weaker consumer wallet, further downtrading, and significant cost pressures. On downtrading, we expect to see a reversal in the mainstream segment as the population of middle-income earners continues to shrink. Notably, the mainstream segment grew for the first time in at least five years in 2019, albeit marginally (+2.0%). We expect brewers to continue to drive their premiumisation strategies in order to improve product-mix and cushion the negative margin impact from the preceding. Overall, volume growth in 2021 should outperform 2020, due to the low base. Beyond that, however, volume growth is expected to be weak.

In our view, the environment is not right for strong price increases on consumer discretionary products. However, we do expect brewers to take sub-inflationary price increases at intervals throughout 2021. NB has already stated that single-digit price increases are expected across key products in December, similar to last year. This should offer slight respite to topline. **Overall, we are Underweight the sector.**

Food & HPC

A Mixed Bag: Consumer Goods stocks mostly underperformed the broader market in terms of returns. The weak performance was due to the demand destruction and consumer income pressure brought about by the pandemic. However, the agro-allied stocks in sugar and salt fared better than the packaged

food and household products names, as well as the brewers. In our view, this was due to their ability to fully price in movements in international prices and currency depreciation into their products. We also attribute the better to performance to relatively more robust volumes on FGN COVID-19 palliative purchases. For the rest of the industry, price remains the main criteria for the consumer, with quality in second place. Consequently, the ability to raise prices above inflation remains constrained.

An Even Steeper Road to Recovery: Consumer spending is expected to remain subdued while market competition will remain intense with consumers increasingly price sensitive. We expect that only innovative companies will outperform. In 2021FY, we are neutral on the overall sector. However, we do have some high conviction names in DANGSUGAR and NASCON. We expect the margins of these companies to remain resilient as they are able to take much larger price increases than peers. On returns, we feel the valuations for these stocks are undemanding compared to historical levels. Additionally, they offer very attractive dividend yields.

Telecoms

Resilient Earnings amidst Pandemic: Nigeria-listed telcos have led their SSA peers this year in terms of returns, as earnings have proven to be resilient amidst the shock of the COVID-19 pandemic. Despite the macro weakness, MTN Nigeria (MTNN) and Airtel Africa (AIRTELAFRI) have both enjoyed strong subscriber growth, increased smartphone and data penetration, and higher 4G population coverage in Nigeria. Both telcos have also continued to invest heavily in infrastructure to expand their reach and subscriber bases, even amidst the currency weakness and FX illiquidity issues. Amidst the challenging macros, and the unattractive yields in the fixed income market, investors have flocked to the and equities market telco stocks to generate alpha. Notably, foreign investors have also taken advantage of the fungibility of AIRTELAFRI and used the stock to exit the Nigerian market amidst the country's FX liquidity issues. As a result, MTNN and AIRTELAFRI share prices have risen 52.4% and 159.1% YTD respectively, as at December 18 and are in the Top 20 best-performing stocks on the NSE. Their SSA peers, on the other hand, are yet to recover from the heavy selloffs in March.

COVID-19 Impact: In these unprecedented times, the telecoms industry has emerged as a key and essential service across Africa. Mobile services have become an affordable alternative for travel and communication during the pandemic, allowing customers to work remotely, reduce their travel, keep them

connected and access affordable entertainment. Although voice traffic declined during the lockdown in Q2, data accelerated on the preceding. According to the Q2 Ericsson Mobility Report, Nigeria (+6 million) recorded the second largest number of subscriber net additions in the world during the quarter, after China (+6 million). Traffic normalised following the removal of the restrictions in Q3, with voice traffic recovering and data continuing to grow on the rising number of smartphone subscriptions and an increasing average data volume per subscription.

Market Share Update – MTNN Is Surging While 9mobile Is Flagging: MTNN has consolidated its market leadership this year, as it is the only telco that has gained subscriber market share in 2020 according to the latest NCC data (October 2020). MTNN's share of mobile subs has grown by 279bps YTD to 40.1%, underpinned by the expanded customer acquisition touchpoints, and rural telephony initiatives implemented in the year, according to management. The story is different for data subscribers, as MTNN's share declined slightly by 47bps to 42.6%. Globacom (not listed) is the only telco that gained data share (+284bps to 25.9%), which in our view, was driven by the company's aggressive promotional prices on data plans. AIRTELAFRI's market share has been relatively flat across both mobile subs (-13bps) and data subs (-74bps). Elsewhere, 9mobile has continued to haemorrhage subscribers, with its share of mobile subs (-116bps) and data subs (-163 bps) declining significantly.

Looking Ahead – Demographic & Structural Upsides: Over the medium to long term, the growth of Nigeria's subs will continue to be underpinned by its attractive demographics as well as structural upsides. From a demographic perspective, Nigeria has a vibrant telecoms market, supported by its estimated 201 million population size and growth rate (c. 3.0% p.a), high urbanisation rate and young population. Furthermore, competition among the leading companies will continue to put intense downward pressure on prices, making telecoms services more affordable.

On our near-term view, we project Nigeria's 2020E and 2021E mobile subs at 209.0 million (+13.3% y/y) and 225.1 million (+7.7% y/y), mobile penetration at 101/3% and 106.4%, and data subs at 155.1 million (+23.4% y/y) and 172.9 million (+11.5%). Beyond that, we forecast mobile subs to grow at a CAGR of 6.8% over 2021-2025E, and data subs to grow at a CAGR of 11.7% over the same period. Amidst intense competition, we expect MTNN to maintain market leadership, with AIRTELAFRI expected to edge out Globacom (not listed) for the second spot.

Risks to our outlook include further shocks to, and weakening of, the consumer wallet, which will negatively impact affordability and consumption of telecom services. The recent regulatory developments around SIM registration is also a significant risk to our subscriber growth outlook.

Mobile Money: The Next Catalyst: MTNN and AIRTELAFRI have applied for the PSB license and according to the management of both companies, are confident they will receive an Approval-In-Principle (AIP), the first stage in the process. However, no time frame was given for this. Currently, MTNN has received a super-agent license, which enables the company to extend the reach of its delivery channels by expanding its agent network while it waits for the PSB license. The super-agent license allows the company to re-purpose its network of agents that sell prepaid airtime also to offer cash-in-cash-out financial services. Its limitation is that it does not enable MTNN to offer prepaid wallets holding e-money.

We expect that like any other product/services, mobile money will be defined by the product's relative value, convenience and safety. On this basis, there is scope for competition via innovation, distribution and the platform. Noteworthy, however, is that regulatory data from Kenya, Tanzania and Ghana suggests that the voice market share leader is also the mobile money market share leader. In fact, the mobile money market share of the leader is higher than voice share. MTN Ghana's management estimates that it accounts for 94% of Ghana's mobile money transaction value and has a mobile money subscriber share of 74% (2019FY conference call). These, in our view, supportive of MTNN ahead of its approval to launch (MTNN is the voice leader with 40.1% market share as of October 2020, according to NCC data).

MTNN (BUY; TP: NGN202.21) remains our top pick in the sector. We expect the company to deliver double-digit topline and bottom-line growth of 15.1% and 30.3% in 2021E, respectively. Our view on (1) continued subscriber growth and network expansion, and (2) recovery in ARPU as the economic effect of the pandemic dissipates, underpins our expectation for the strong performance. Our TP implies an attractive 26.4% upside for the stock. Incorporating our 2021E dividend yield expectation into our total expected return gives us a return of 33.0%.

Oil & Gas - Downstream

Pandemic crushed demand: Petroleum products demand, which has been stable in recent years, wavered in April and May, as the lockdown negatively impacted economic and social activities. Consequently, demand from heavy petroleum

products consuming sectors such as road transportation and aviation slumped due to restrictions on road movement and air travel. Unsurprisingly, the aviation and road transport sectors recorded GDP declines of 57.4% and 51.4% respectively, in Q2-20, according to the National Bureau of Statistics (NBS). Disruptions across significant industries such as manufacturing and services, which rely on petroleum products for power generation, also contributed to the decline in demand.

Higher prices, better margins: Notably, in the face of the pandemic, the federal government (FG) announced the liberalisation of the price of PMS. With oil prices plunging to a multi-decade low of USD19.33/barrel, and PMS landing cost falling from NGN121.65/litre in February to NGN64.33/litre in March, the FG exploited the window to adopt market-reflective pricing for the product. The FG reviewed the PMS pump price downwards, for the first time since 2015, to NGN125.00/litre from NGN145.00/litre. With this new template, the PPPRA determined the price of PMS monthly. However, in September 2020, the PPPRA fully liberalised the price of the product, as it announced that it would no longer set a price band for the product going forward. Although the price liberalisation is yet to be backed by law, the action is a big positive for oil and gas marketers, as they can now grow the margin on the product. The impact has already begun to show in the results of some of the listed product marketers. Looking at 9M-20 numbers, TOTAL (+260bps y/y to 13.9%), ARDOVA (+39bps y/y to 7.0%), ETERNA (696bps y/y to 8.7%) and MRSOIL (86bps y/y to 7.0%) all recorded gross margin growth compared to last year.

Higher prices and demand to boost marketers' revenue: Our key themes for the sector in 2021 include (1) higher petroleum product prices, (2) improved demand, (3) continued supply from the NNPC, (4) the government's efforts to boost Autogas adoption, and (5) the passage of the Petroleum Industry Bill (PIB).

We forecast PMS price to average between NGN165.00/litre and NGN175.00/litre in 2021. Our view is hinged on our higher average oil price assumption (USD45.00 - USD50.00/bbl) in 2021. With higher oil prices, we expect better revenue outturn for downstream oil and gas marketers.

As the economy has effectively reopened, we expect demand for products to return to pre-pandemic levels. Furthermore, Nigeria's continued heavy reliance on fossil fuels for energy consumption accentuates our view. However, we note that a second wave of the virus poses a significant downside risk for product demand.

Despite the FG's push for increased Autogas adoption, we do not expect a significant shift from the status quo. The idea is laudable as Autogas is cheaper (government estimate: NGN97.00/litre), compared to PMS, and environmentally friendly. In our view, however, it will be a herculean task to hit the government's one million vehicle conversion target by the end of 2021. Firstly, it costs between NGN300,000 (USD790.00¹) to NGN450,000 (USD1185.00¹) per conversion. Although the government indicated it would charge NGN250,000 (USD658.00¹) per conversion, the reduced fee is still unaffordable for many consumers, owing to the negative impact of real wage declines, surging inflation, and high unemployment. Secondly, Autogas dispensing facilities have to be readily available across a significant number of service stations. Currently, only 27% of retail stations in Nigeria have are suitable for integration of Autogas add-on facilities, according to the DPR. Managements of downstream players we spoke to have indicated a willingness to develop their retail outlets to accommodate Autogas dispensing but only on the condition that there is a defined framework on how the government intends to introduce the use of the product. Overall, we do not expect significant growth in Autogas adoption in the short-to-medium term.

On supply, NNPC's recent tender seeking to select companies to participate in the 2021 – 2022 DSDP swap programme, indicates that the NNPC will hold on to its monopoly in the supply side of the market until at least 2022 when the Dangote Refinery comes onstream. We expect individual product sourcing to remain challenging for oil and gas marketers, following the foreign exchange illiquidity in the country.

Regardless of the PMS price liberalisation, there is still a need for a law to back downstream market operations to ensure efficiency. Hence the clamour for the PIB. Given the current rosy relationship between the executive and legislative arms of government, we expect the bill to be passed in 2021. We expect the bill to foster the growth and investment that the oil and gas space has been lacking for the past few decades. We highlight that full deregulation will attract the capital for investments needed to revamp the downstream sector. Funding for investments such as the rehabilitation and maintenance of refineries, pipelines, depots, among others, will be easy to come by.

Against the preceding, our top pick for the sector is TOTAL (BUY, TP: NGN147.94). TOTAL remains the dominant player in the downstream subsector of the Oil & Gas industry, with a robust distribution network – over 560 outlets – representing about c.23% share of outlets controlled by major

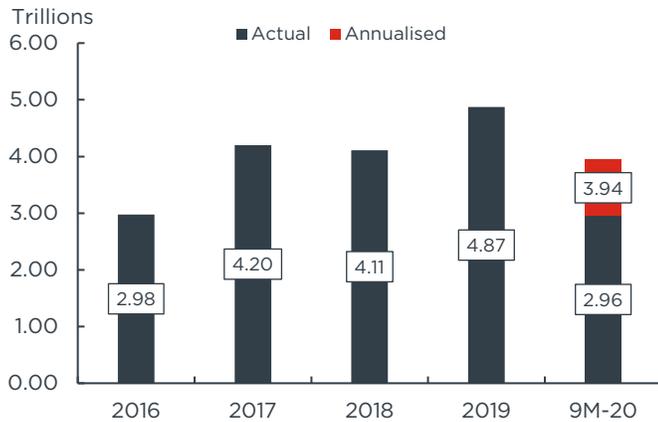
¹ Converted at official Exchange rate; USD1.00 = NGN380.00

marketers. Slightly higher PMS prices next year in addition to its substantial white product volumes will help to boost revenue in 2021. We also like the company's continued drive to improve its sales-mix and margins – the company has plans to further expand capacity (2019:76kT) in the higher-margin lubricant segment where it is the market leader. Additionally, the company has put inventory and price risk management at the core of its strategy. In our view, this will be highly critical in optimising margins and working capital going forward as, due to the deregulation, PMS prices are now linked to volatile oil prices on the international markets.

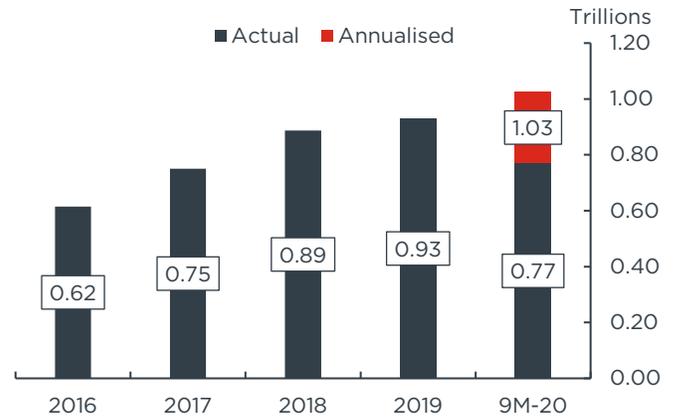
On returns to shareholders, TOTAL has consistently paid dividends since 2006, with a dividend payout of 82% on average over the last 14-year period. We expect this continue going forward, given our view on improved earnings and cash flow generation.

Chart Pack. *Financials - Banking.*

Gross Earnings Trend 2016 - 9M-20 (NGN)

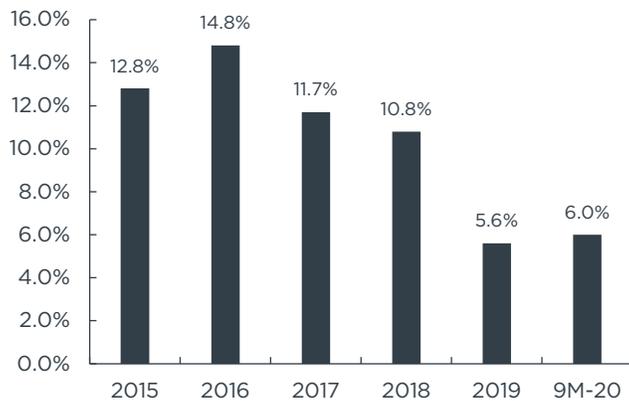


Profitability Trend 2016 - 9M-20



Source: Company Financials, Cordros Research

Non-performing Loans Trend 2016 - 9M-20



Cost-to-Income ratio Trend 2016 - 9M-20

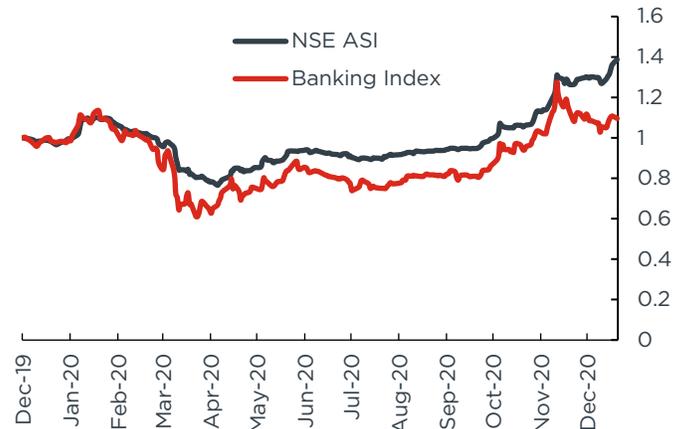


Source: NBS, Company Financials, Cordros Research

Liquidity Ratio Trend 2016 - 9M-20



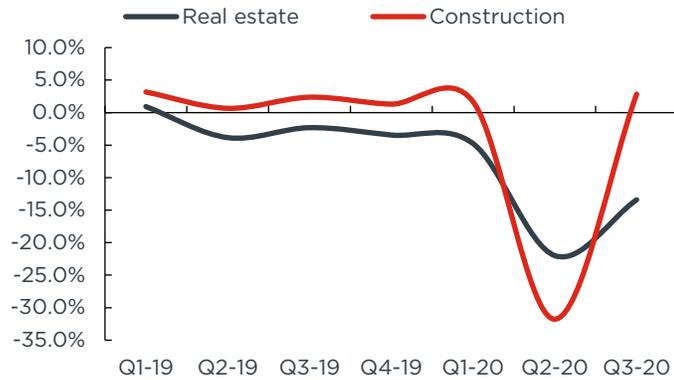
NSE-ASI vs NSEBANK-10 (1-year Trend)



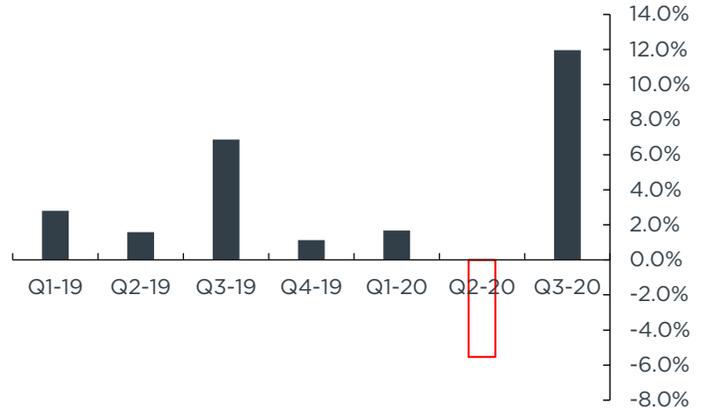
Source: NSE, Company financials, Cordros Research

Chart Pack. *Cement.*

Real estate and Construction sectors GDP (%)

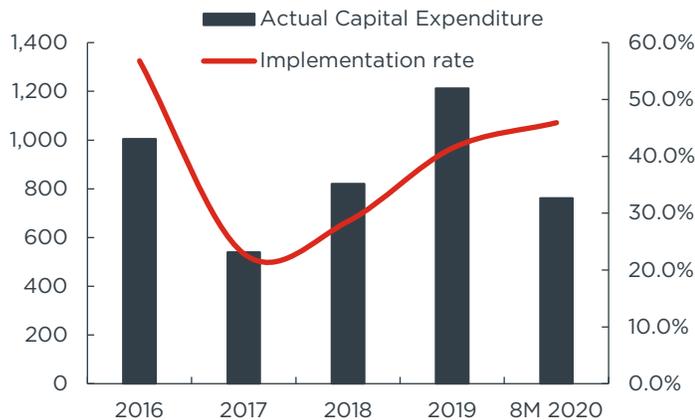


Cement sector GDP (%)

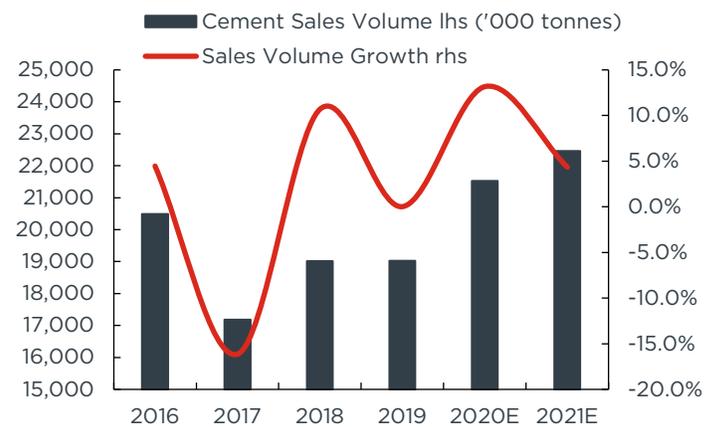


Source: NBS, Cordros Research

Actual CAPEX and Performance ratio (%)

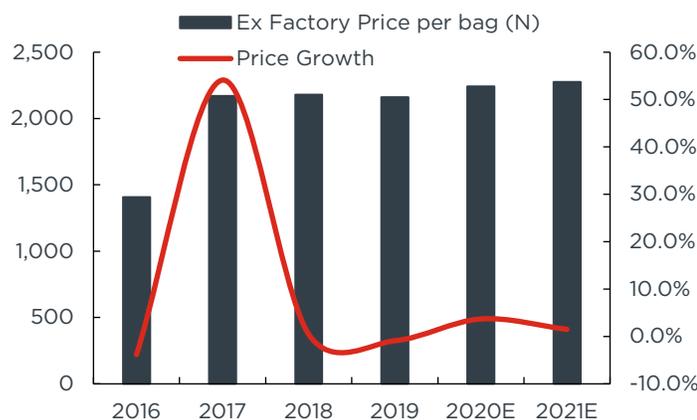


Cement sales volumes and growth rate (%)



Source: Ministry of Budget, Company Financials, Cordros Research estimates

Ex-factory price and growth rate (RHS,%)



Real estate sector GDP (%)



Source: NBS, Cordros Research estimates

Chart Pack. *Consumer Staples - Agriculture.*

Global CPO price (USD/mt)

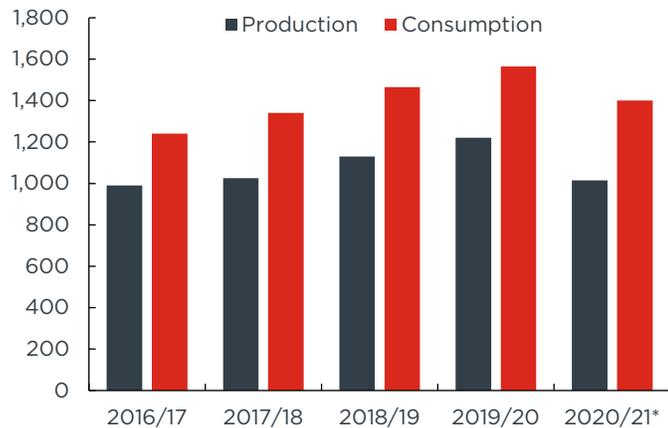


Global rubber price (USD/kg)



Source: Bloomberg, Cordros Research

CPO Production/Consumption in Nigeria (mt '000s)

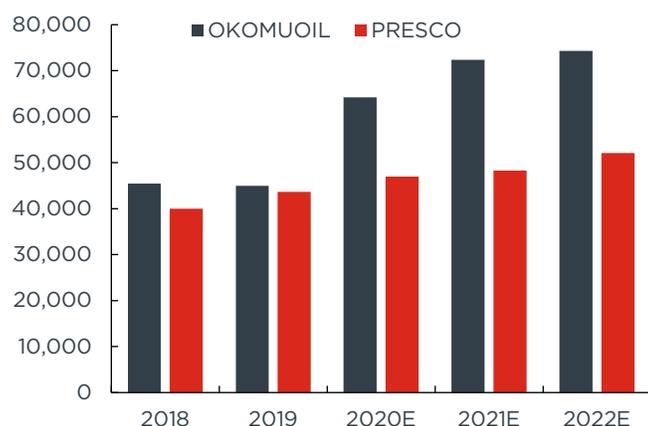


Refined palm oil price (per litre) in Nigeria (NGN)

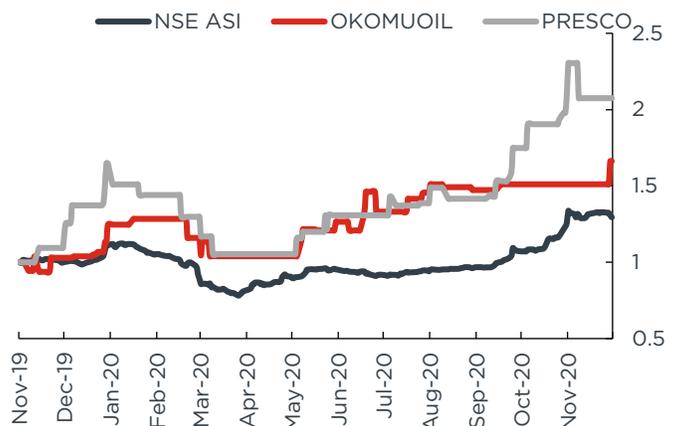


Source: USDA, NBS, Cordros Research | *as of November 2020

OKOMUOIL and PRESCO CPO volumes (tonnes)



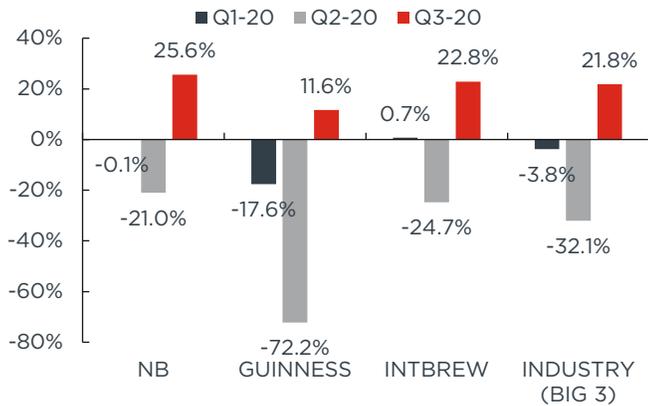
Performance of our focus companies vs the broader ASI



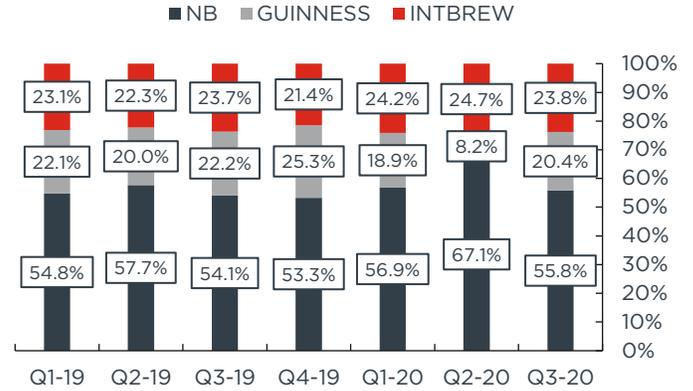
Source: NSE, Company financials, Cordros Research

Chart Pack. *Consumer Staples - Brewers.*

Net Revenue Growth (year-on-year)

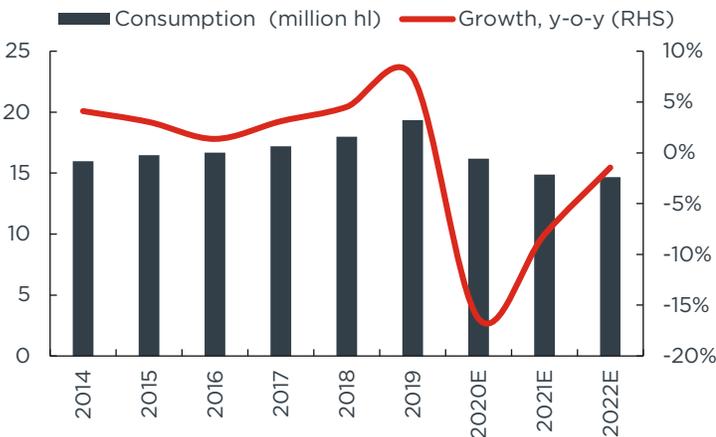


Net revenue market share (Big 3)

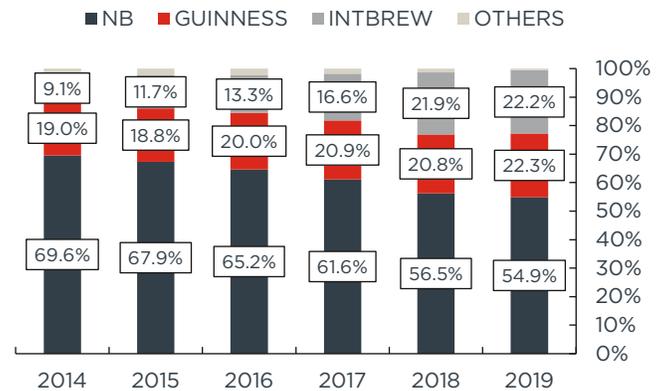


Source: Company financials, Cordros Research | GUINNESS year-end is in June; figures represent calendar quarters

Nigeria Beer Consumption

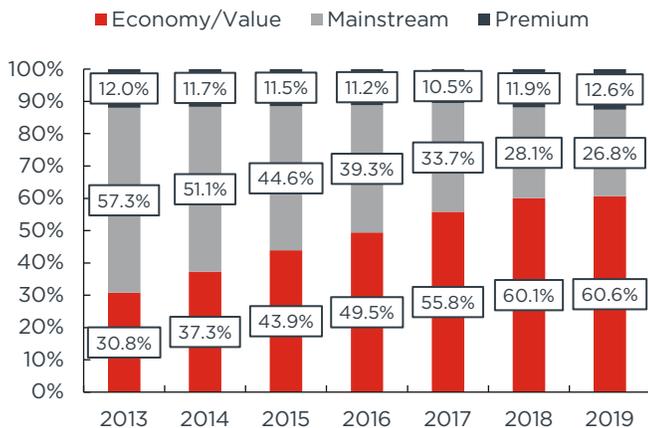


Beer Volume market share

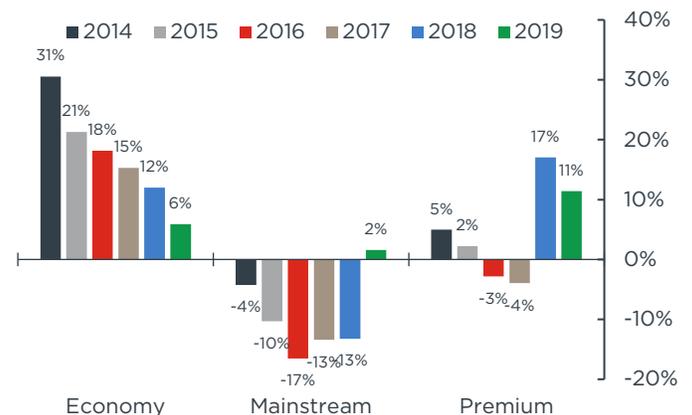


Source: Euromonitor, Cordros Research

Value market share by segment (Beer)



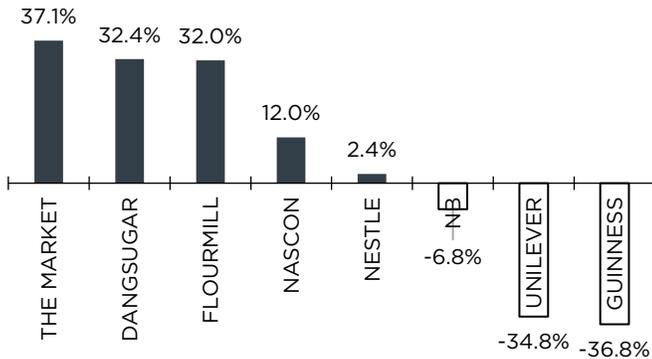
Volume growth by segment (Beer)



Source: Euromonitor, Cordros Research

Chart Pack. *Consumer Staples – Food & HPC.*

YTD share performance of individual stocks (%)

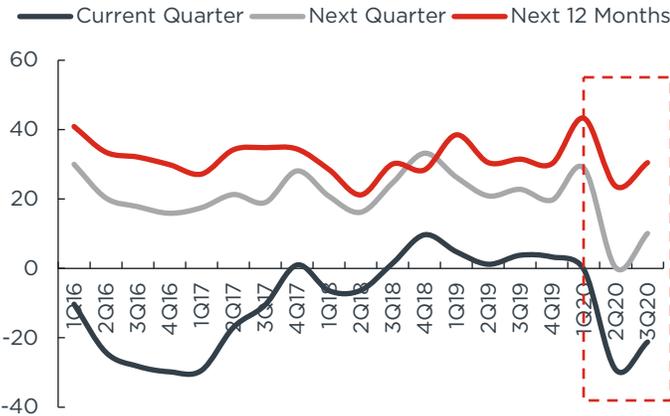


Benchmark indices: YTD performance (rebased to 1)

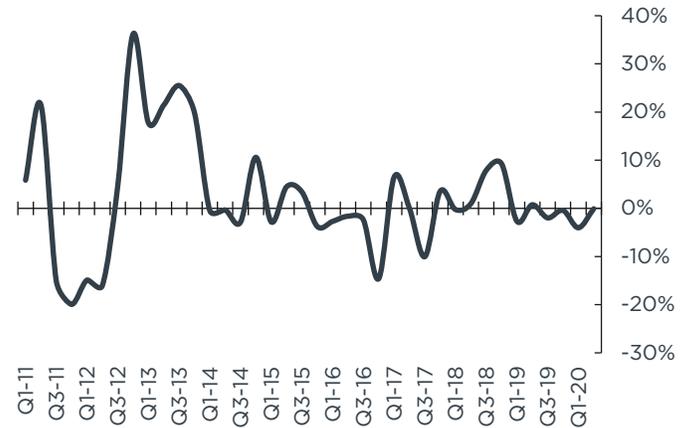


Source: NSE, Cordros Research

Consumer Expectations Survey (points)

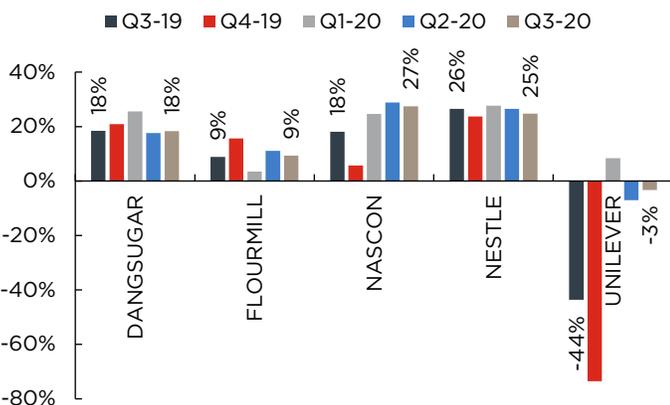


Real Final Household Consumption (y/y growth)

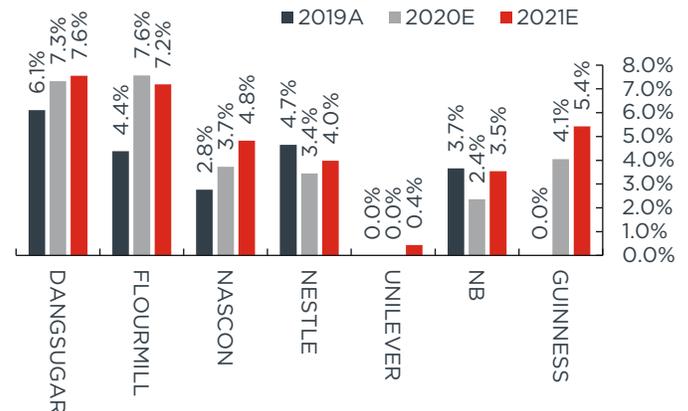


Source: CBN, NBS, Cordros Research

LFL EBITDA margins (Q3-19 to Q3-20)



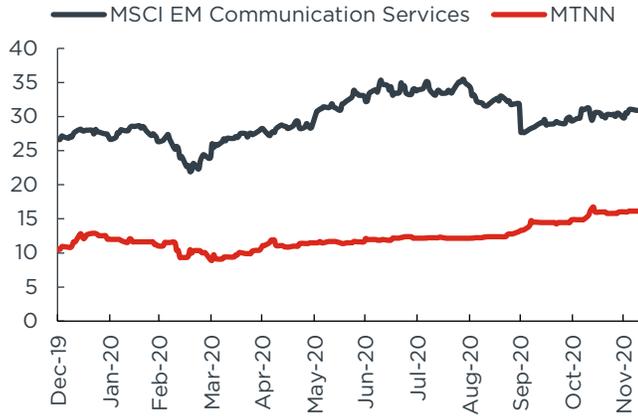
Dividend yield (actual & estimates)



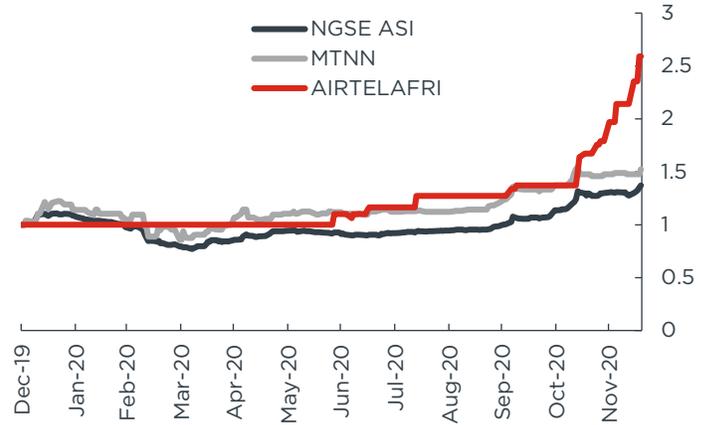
Source: Company financials, Cordros Research estimates | *FLOURMILL and GUINNESS have Mar and June year ends, respectively

Chart Pack. *Telecoms.*

TTM P/E Ratios (x)

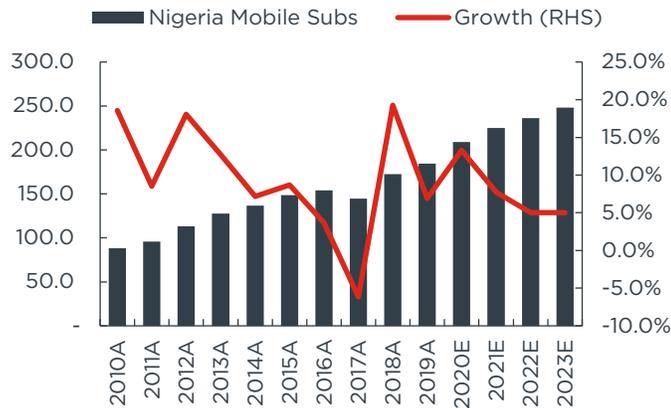


YTD share price performance (rebased to 1)

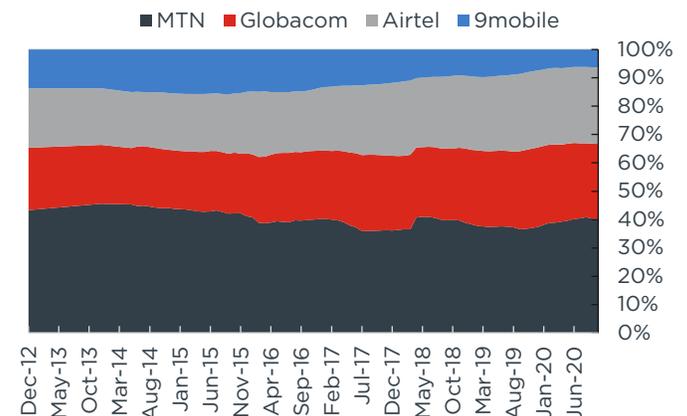


Source: Bloomberg, NSE, Cordros Research

Nigeria Mobile Subscribers (millions)

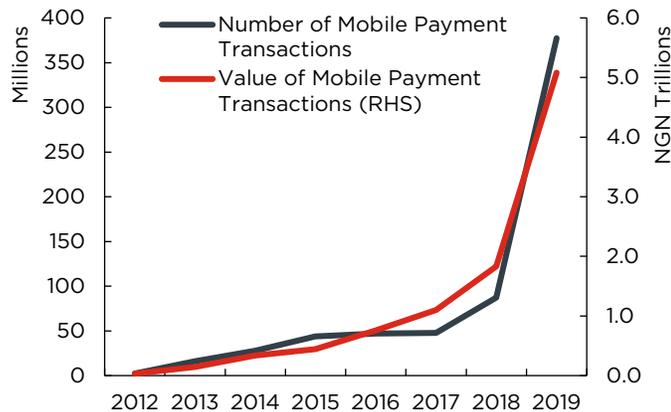


Nigerian Telcos: Subscriber Market Share

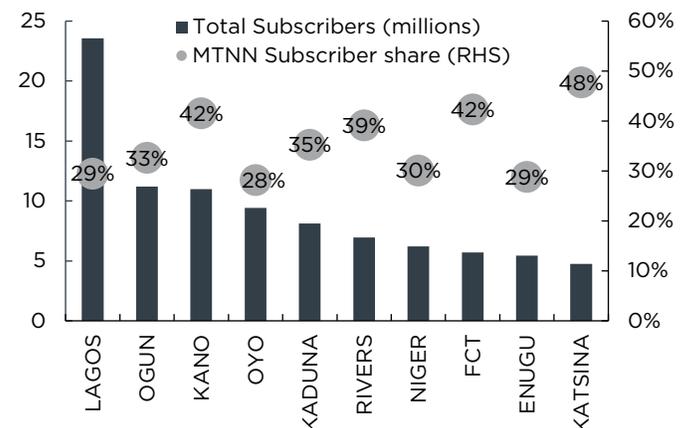


Source: NCC, Cordros Research estimates

Nigeria - Mobile Money Statistics



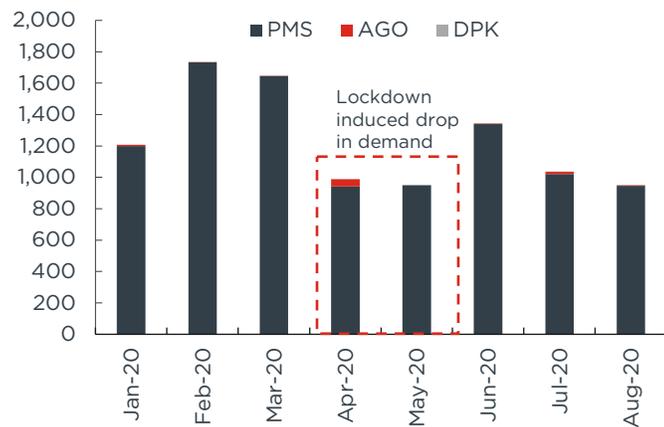
MTNN subscriber share in the Top 10 states



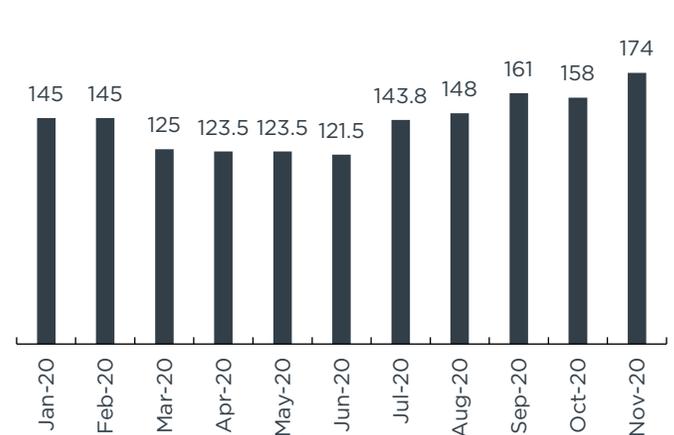
Source: CBN, NBS, Cordros Research estimates

Chart Pack. *Oil & Gas.*

White product demand in Nigeria (million litres)

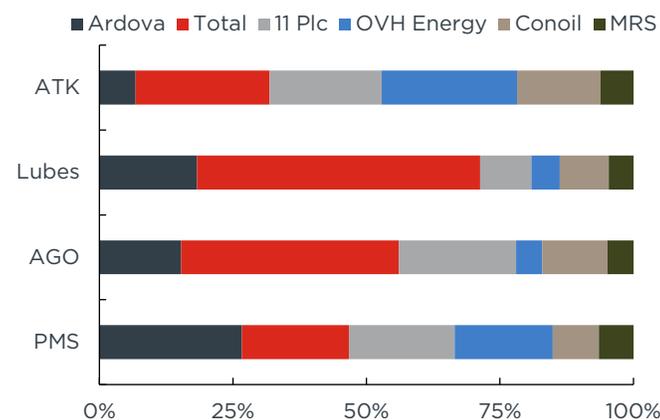


Monthly PMS price in 2020 (NGN)

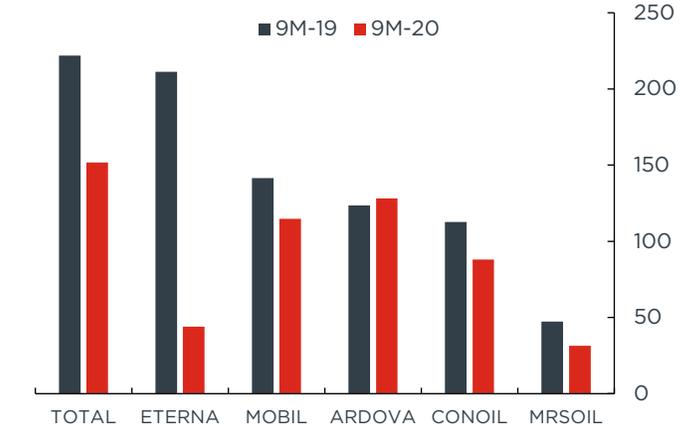


Source: NNPC, PPPRA, Cordros Research

MOMAN market share data

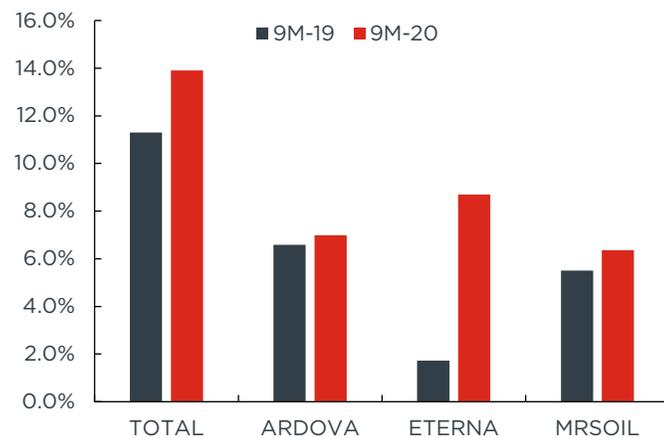


Revenue of listed oil & gas marketers (NGN billion)

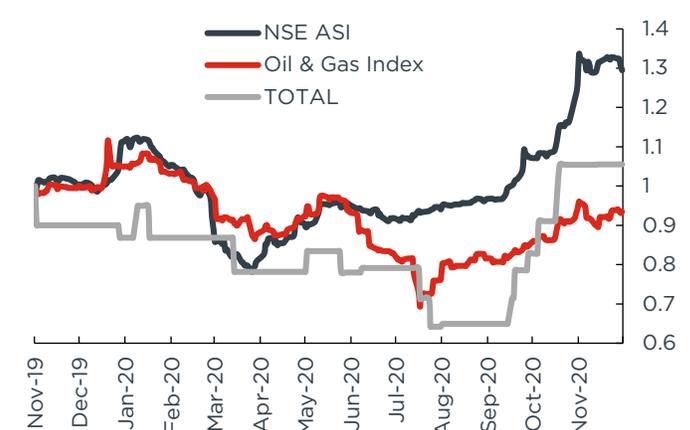


Source: MOMAN, Company financials, Cordros Research

Improved gross margins of selected marketers



Share performance of our sector top pick



Source: Company financials, NSE, Cordros Research

Appendix.

Nigeria. Key Economic Forecasts.

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020E	2021E
Activity													
Real GDP (% YoY)	8.4	9.5	5.3	4.2	5.5	6.2	2.8	(1.6)	0.8	1.9	2.3	(3.5)	2.0
Private consumption (% YoY)			2.6	0.3	29.3		(0.3)	11.9	9.8	5.2	9.9	(4.5)	(2.1)
Government consumption (% YoY)	(8.1)	17.8	4.6	(2.0)	(10.3)	(7.0)	(0.4)	(2.2)	(3.8)	24.2	12.2	71.6	22.3
Oil production (million b/d year-end)	2.1	2.4	2.4	2.0	2.2	2.2	2.1	1.6	1.9	1.9	2.0	1.7	1.8
Nominal GDP (NGN billion)	44,286	54,612	62,980	71,714	80,093	89,044	94,145	101,489	113,712	127,737	144,210	158,584	188,210
Nominal GDP (USD billion)	292	363	410	459	515	569	495	405	376	398	448	441	495
Real GDP (NGN billion)	49,856	54,612	57,511	59,930	63,219	67,153	69,024	67,931	68,491	69,800	71,388	69,403	70,776
Population (million)	155	160	165	170	176	181	187	193	199	205	211	218	224
GDP per capita (USD)	2,180	2,292	2,350	2,385	2,477	2,564	2,563	2,456	2,412	2,396	2,387	2,023	2,209
Gross national saving (% of GDP)	23.2	10.9	10.4	11.2	10.8	13.5	12.2	12.1	11.4	11.8	11.8		
Stock of bank credit to the economy (NGN billion)	8,912	7,706	7,313	8,150	10,006	12,889	13,086	16,117	15,741	15,134	17,188	20,603	21,396
Stock of bank credit to the economy (% of GDP)	20.1	14.1	11.6	11.4	12.5	14.5	13.9	15.9	13.8	12.1	11.1	13.0	11.4
Loan to deposit ratio (%)	85.7	74.2	44.8	42.3	38.0	64.2	69.6	80.0	78.2	64.3	59.9	65.0	65.0
Fiscal balance (% of GDP)													
Federal government balance	(1.8)	(2.0)	(1.8)	(1.4)	(1.4)	(0.9)	(1.7)	(2.6)	(3.2)	(2.8)	(3.4)	(4.0)	(4.5)
Total public debt	9.6	9.6	17.6	17.7	18.6	17.5	20.3	23.4	25.3	28.4	19.9	22.6	25.4
Capital Expenditure	2.6	1.6	1.5	1.0	1.1	0.7	0.6	0.2	1.3	1.3	0.8	0.8	1.3
Debt Indicators													
Gross external debt (USD billion)	3.9	4.6	5.7	6.5	8.8	9.7	10.7	11.4	18.9	25.3	27.7	31.9	35.7
Gross external debt (% of GDP)	1.3	1.1	1.1	1.0	1.1	1.1	2.0	2.6	3.0	4.7	5.6	7.3	7.2
Gross external debt (% of exports)	6.7	5.7	5.7	6.7	9.0	11.7	23.3	32.9	41.3	41.3	42.6	88.6	98.6
Total debt service (USD billion)	1.7	2.8	3.4	4.3	5.3	5.9	5.5	5.6	6.0	7.1	8.0	8.4	8.7
Total debt service (% of GDP)	0.6	0.8	0.8	0.9	1.0	1.0	1.1	1.4	1.6	1.8	1.8	1.9	1.8
Total debt service (% of exports)	2.9	3.4	3.4	4.4	5.4	7.2	12.0	16.2	13.0	11.5	12.3	23.3	24.0
External Balance													
Exports (NGN billion)	7,435	13,010	19,036	22,446	14,245	16,304	9,593	8,527	13,598	18,532	19,192	12,556	17,681
Exports (USD billion)	58.2	80.6	99.9	97.0	97.8	82.6	45.9	34.7	45.8	61.2	65.0	36.0	36.2
Imports (NGN billion)	5,048	6,649	10,033	5,625	7,016	7,374	6,698	8,818	9,563	13,165	16,960	17,646	16,826
Imports (USD billion)	33.9	44.2	65.2	35.7	44.6	46.5	34.7	34.8	31.3	43.0	55.3	43.2	40.1
Trade balance (NGN billion)	2,387	6,361	9,003	16,821	7,229	8,930	2,895	(290)	4,036	5,367	2,232	(5,090)	855
Trade balance (% of GDP)	5.4	11.6	14.3	23.5	9.0	10.0	3.1	(0.3)	3.5	4.2	1.5	(3.2)	0.5
Current account balance (USD billion)	14.0	14.6	12.7	18.9	20.1	1.3	(15.4)	2.7	10.4	5.3	(17.0)	(17.6)	(22.6)
Current account balance (% of GDP)	5.3	4.0	3.1	4.1	4.0	0.2	(3.2)	0.7	3.0	1.5	(3.6)	(4.0)	(4.5)
Net FDI (USD billion)	7.1	5.2	8.1	8.1	4.4	3.1	1.6	3.1	2.2	0.6	1.8	0.5	1.4
Net FDI (% of GDP)	2.7	1.4	2.0	1.7	0.9	0.6	0.3	0.8	0.6	0.2	0.4	0.1	0.2
Current account balance plus FDI (% of GDP)	8.0	5.4	5.1	5.8	4.8	0.8	(2.9)	1.5	3.7	1.7	(3.2)	(3.2)	(3.4)
Exports (% YoY, NGN value)	(22.3)	75.0	46.3	17.9	(36.5)	14.5	(41.2)	(11.1)	59.5	36.3	3.6	(34.6)	40.8
Imports (% YoY, NGN value)	53.0	31.7	50.9	(43.9)	24.7	5.1	(9.2)	31.6	8.5	37.7	28.8	4.0	(4.6)
Foreign exchange reserves (ex. gold, USD billion)	42.4	32.3	32.6	43.8	42.8	34.2	28.3	27.0	39.4	42.6	38.1	34.5	30.2
Foreign exchange reserves adequacy (months of imports)	16.4	9.0	6.1	8.6	10.0	7.4	7.0	9.1	12.0	13.8	8.2	8.0	6.8
Prices													
CPI (average % YoY)	12.6	13.8	10.9	12.2	8.5	8.0	9.0	15.6	16.5	12.1	11.4	13.3	16.6
CPI (year-end % YoY)	13.9	11.8	10.3	12.0	8.0	8.0	9.6	18.5	15.4	11.4	12.0	15.8	15.4
Interest & Exchange Rates													
Monetary policy rate (MPR), % year-end	6.0	6.3	12.0	12.0	12.0	13.0	11.0	14.0	14.0	14.0	13.5	11.5	12.0
Broad money supply (NGN billion)	10,781	11,526	13,303	15,481	15,681	18,886	20,030	23,592	24,141	27,069	29,138	34,033	35,769
Broad money supply (% YoY)	17.6	6.9	15.4	16.4	1.3	20.4	6.1	17.8	2.3	12.1	7.6	16.8	5.1
Credit to the private sector (NGN billion)	10,219	9,830	14,184	15,152	16,191	18,126	18,721	21,982	22,291	22,708	26,637	30,739	31,692
Credit to the private sector (% YoY)	26.8	(3.8)	44.3	6.8	6.9	11.9	3.3	17.4	1.4	1.9	17.3	15.4	3.1
3-month interest rate (T-bill year-end %)	4.3	7.5	14.1	11.7	10.9	10.8	5.7	21.0	14.0	11.3	5.2	0.3	0.2
5Y yield (% year-end)	9.4	12.0	11.2	12.0	13.3	15.3	11.0	11.4	14.0	15.2	10.3	2.1	5.0
Official exchange rate, (NGN/USD) year-end	148.1	148.8	156.7	155.8	155.7	168.0	197.0	305.0	306.0	307.0	307.0	380.0	400.0
Official exchange rate (NGN/USD) annual average	148.9	150.3	153.9	157.5	157.3	158.6	193.3	253.5	305.8	306.1	306.9	357.0	389.3
BDC exchange rate (NGN/USD) annual average	161.6	153.1	159.3	160.9	162.4	171.5	222.7	372.9	395.4	361.5	359.5	435.3	453.0
BDC exchange rate (NGN/USD) year end	155.0	156.0	165.0	159.0	172.0	191.5	267.0	490.0	363.0	361.0	362.0	475.0	450.0
I & E exchange rate (NGN/USD) annual average									365.6	362.1	361.9	381.5	404.8
I & E exchange rate (NGN/USD) year end									360.3	364.0	364.5	395.0	415.0

Source: World Bank, CBN, NBS, Cordros Research estimates

Coverage Universe. *Valuation Summary.*

BANKS	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E (x)	P/B (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
ACCESS	BUY	13.80	8.05	71.4%	3.1	2.6	0.4	2.7	9.3%	80.7%
FBNH	BUY	8.50	6.85	24.1%	2.1	3.3	0.4	3.0	10.2%	34.3%
GUARANTY	BUY	41.07	32.90	24.8%	6.9	4.8	1.3	8.1	8.7%	33.5%
UBA	BUY	11.24	8.00	40.5%	2.4	3.4	0.5	2.4	10.6%	51.1%
ZENITHBANK	BUY	32.28	22.70	42.2%	6.9	3.3	0.7	3.6	12.6%	54.8%
Average				40.6%	4.3	3.5	0.7	3.9	10.3%	50.9%

INDUSTRIAL GOODS	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E(x)	EV/EBITDA (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
DANGCEM	BUY	252.68	183.00	38.1%	14.9	12.2	6.8	10.5	7.8%	45.8%
WAPCO	BUY	29.53	20.55	43.7%	1.4	14.3	4.3	10.6	5.8%	49.5%
Average				40.9%	8.2	13.3	5.5	10.6	6.8%	47.7%

CONSUMER GOODS	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E(x)	EV/EBITDA (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
FOODS										
DANGSUGAR	BUY	26.36	17.75	48.5%	2.8	6.3	3.9	7.8	7.7%	56.2%
FLOURMILL	BUY	31.24	24.70	26.5%	NA	NA	3.4	6.6	9.3%	35.8%
NESTLE	HOLD	1326.57	1400.00	-5.2%	51.4	27.2	14.7	23.4	4.3%	-1.0%
NASCON	BUY	20.49	16.00	28.1%	1.5	10.4	6.5	14.2	4.4%	32.4%
Average				24.5%	18.6	14.6	7.1	13.0	6.4%	30.9%

BREWERS	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E(x)	EV/EBITDA (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
GUINNESS	BUY	23.64	17.00	39.1%	-6.0	NA	4.3	15.0	4.0%	43.1%
NB	HOLD	51.33	55.00	-6.7%	1.3	40.8	7.7	28.2	3.5%	-3.1%
Average				16.2%	-2.3	40.8	6.0	21.6	3.8%	20.0%

HOUSEHOLD & PERSONAL CARE (HPC)	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E(x)	EV/EBITDA (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
UNILEVER	HOLD	13.14	12.90	1.9%	-1.2	NA	NA	184.3	0.5%	2.3%

AGRICULTURE	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E(x)	EV/EBITDA (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
OKOMUOIL	HOLD	84.57	88.00	-3.9%	6.7	13.1	6.6	12.6	3.4%	-0.5%
PRESCO	SELL	63.93	71.80	-11.0%	5.2	13.7	7.9	15.0	2.8%	-8.2%
Average				-7.4%	6.0	13.4	7.2	13.8	3.1%	-4.3%

TELECOMMUNICATIONS	Rating	Price Target (NGN)	Price (NGN)	Potential Up/Downside (%)	TTM EPS	P/E(x)	EV/EBITDA (x)	Forward P/E (x)	Div Yield 2020E (%)	Exp. Return (%)
MTNN	BUY	202.21	155.00	30.5%	9.7	16.0	4.6	11.8	6.8%	37.2%

FLOURMILL year-end is in March; GUINNESS year-end is in June | NA = Not Applicable
 Source: NSE, Bloomberg, Cordros Research estimates

Disclosures.

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