CSL Stockbrokers Limited

The Rough Patch to Safety

H2 2021 Macroeconomic Outlook

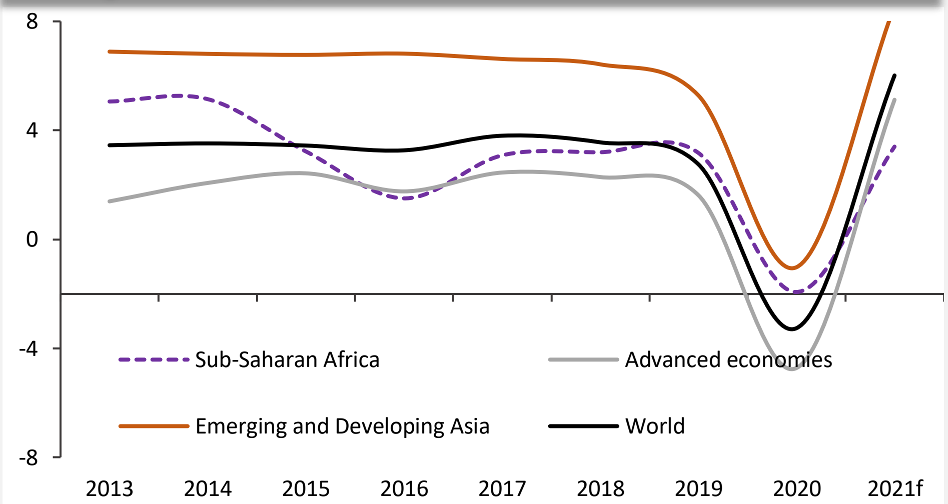
TABLE OF CONTENTS

SECTION 1

GLOBAL/SSA ECONOMIC REVIEW AND OUTLOOK

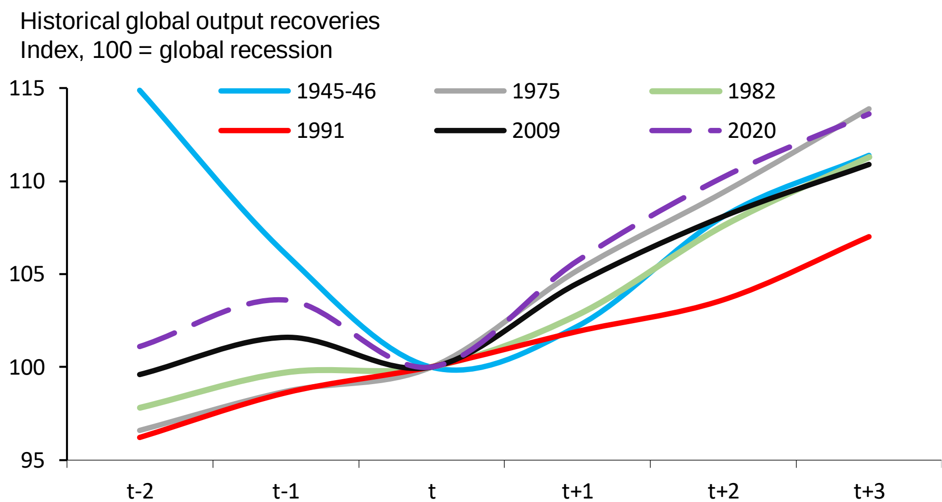
VACCINATION TO DRIVE ECONOMIC RECOVERY, BUT DOWNSIDE RISK ABOUNDS

Global growth rates (%)

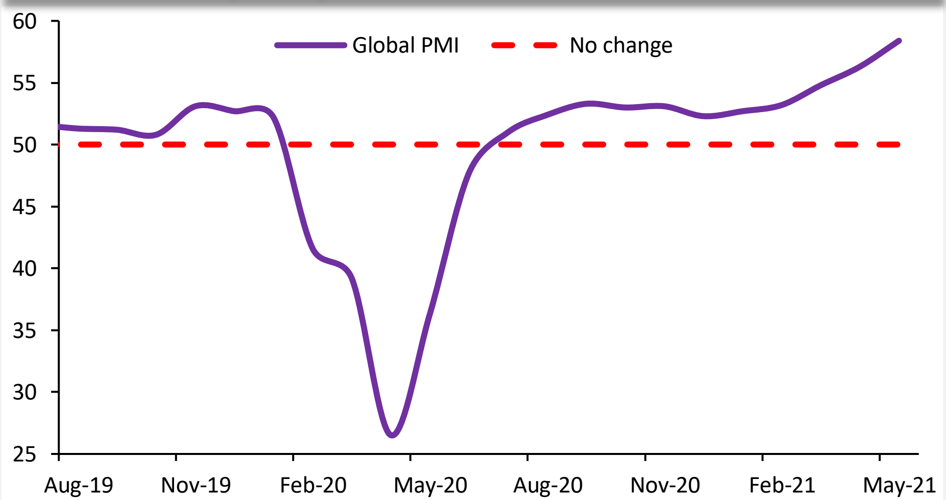


2021 Forecast	GDP (%)	Inflation (%)
World	6.5	3.5
Advanced Economies	5.1	1.6
US	6.4	2.3
Euro Area	4.4	1.4
UK	5.3	1.5
Japan	3.3	0.1
EMDEs	6.7	4.9
China	8.4	1.2
India	12.1	4.9
ASEAN-5	4.9	2.3
Saudi Arabia	2.9	2.7
Russia	3.8	4.5
SSA	3.4	9.8

Strongest post-recession rebound in global output



Global Purchasing Managers' Index (PMI)



Sources: IMF, World Bank, JPMorgan, CSL Research

CSL

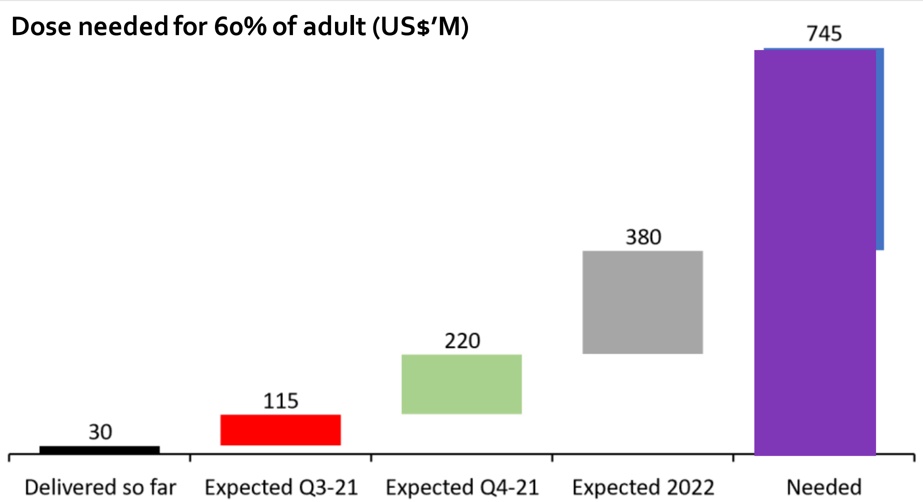
GROWTH IS BIASED TO THE UPSIDE, BUT IS INFLATION THE NEW CONCERN?

Global Economy	The global economy is projected to rebound by 6.0% in 2021, supported by the continued Covid-19 vaccine rollout and dovish monetary stance. However, supply-chain pressures, rising commodity prices and rapid domestic demand in major economies have intensified global inflation pressures. Growth · Inflation · Monetary policy
USA	The U.S. economy grew at 6.4% in Q1 2021, as the combined impact of mass vaccination rollout and federal stimulus triggered a surge in consumer spending. Outlook is positive amid robust consumer spending and manufacturing activity. However, the soaring inflation remains a concern. Growth · Inflation · Monetary policy
EURO AREA	Growth in Eurozone is expected to strengthen to 4.4% in 2021, on the back of broader implementation of fiscal stimulus under the Next Generation EU plan. According to S&P, the Recovery and Resilience Facility (measures to mitigate the economic and social impact of the covid-19) could add 1.3%-3.9% to eurozone GDP over the next five years Growth · Inflation · Monetary policy
Emerging & Developing Asia	Growth is gaining momentum in the region, driven mainly by China. Also, cross border trade has improved, strengthened by global economic activity and rebound in manufacturing. Another wave of the pandemic and potential delays in vaccine rollouts remain a downside to our outlook. Growth · Inflation · Monetary policy

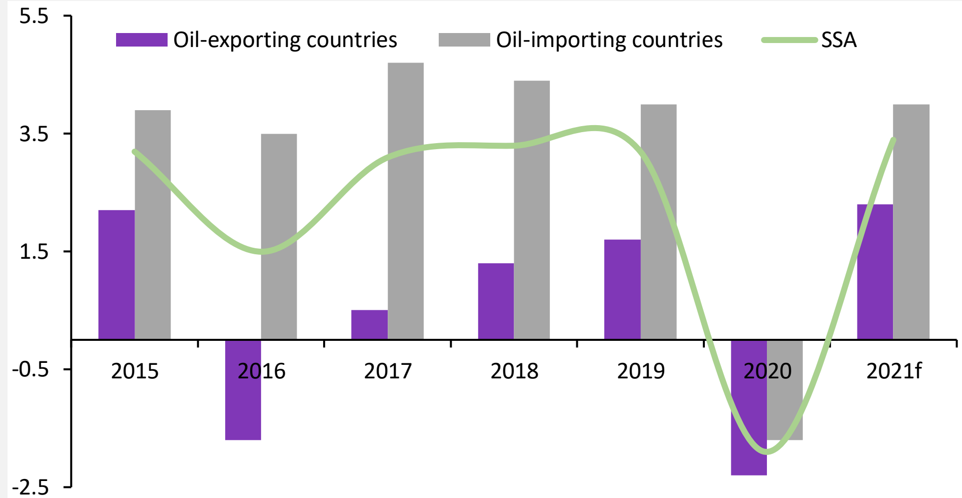
Legend: Lower | Neutral | Higher (over the next 6-month)

SSA GROWTH TO STRENGTHEN IN 2021, DESPITE LOW VACCINATION

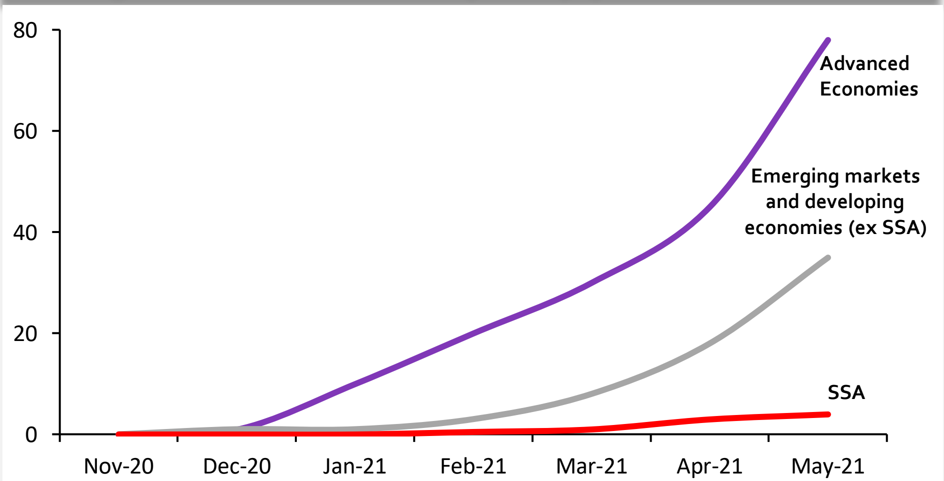
SSA continues to lag in Covid-19 vaccination



SSA GDP growth (%)



Covid-19 vaccine doses administered per 100 population

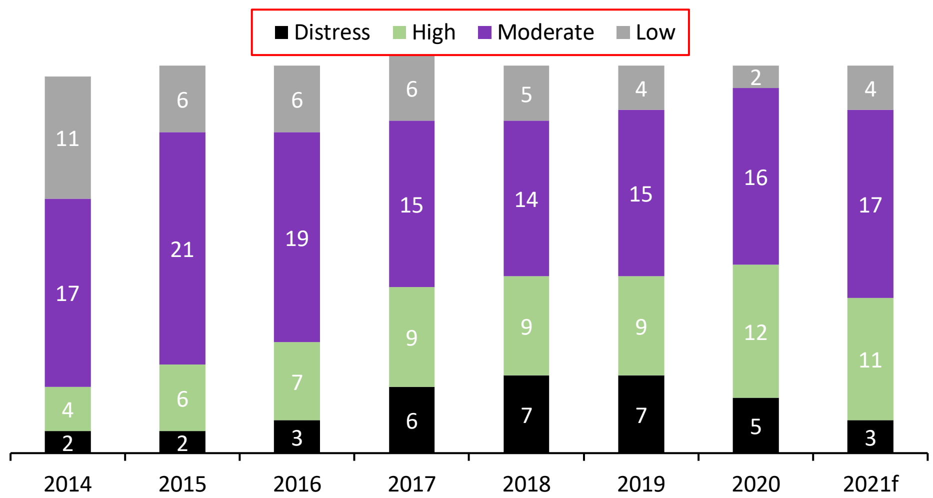


- In 2020, the SSA region slumped to the deepest recession since the 1960s, as output contracted by 2.4%, owing to the Covid-19 pandemic. However, the recession was mild, as the virus spread was slower and agricultural activity was unexpectedly strong in some countries like Benin, Ethiopia, Kenya, Nigeria.
- Growth in the region is projected to reach 3.4% in 2021 driven by stronger external demand from the region's major trading partners (China and the US), higher commodity prices, and better containment of Covid-19.
- Furthermore, domestic consumption is poised to increase, on the back of normalisation of economic activities in heavyweight countries. This confirms the improved PMI readings witnessed in recent months.

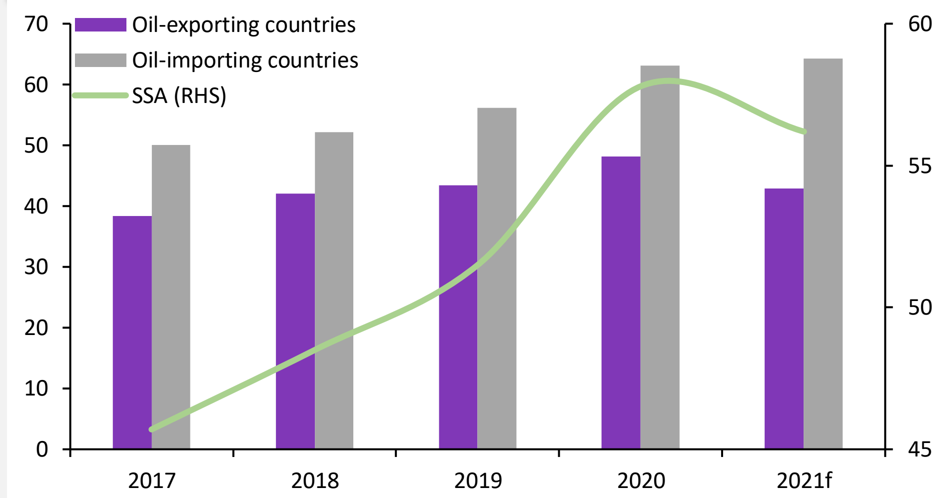
Sources: IMF, CSL Research

RISK OF DEBT DISTRESS TO TAPER IN 2021, SUPPORTED BY ECONOMIC RECOVERY

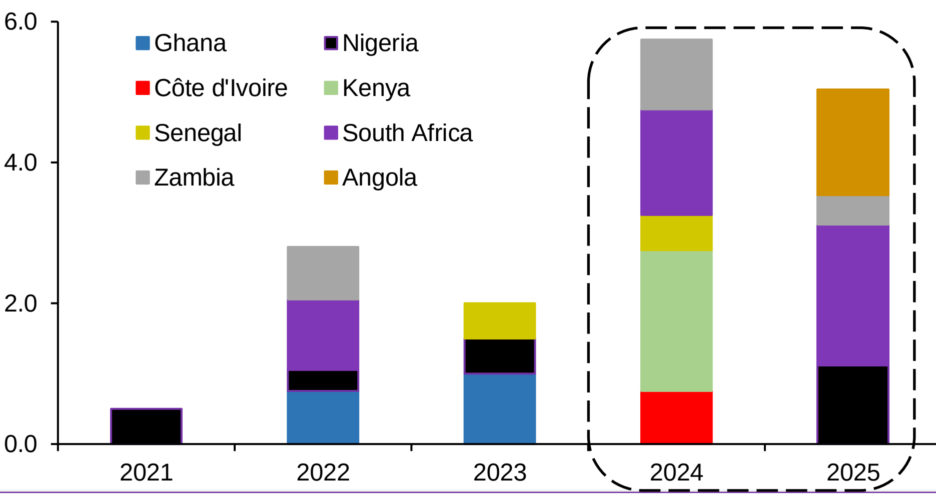
SSA debt sustainability analysis of countries within the region



Government Debt (% of GDP)



SSA Eurobonds maturities (USD bn)



- **2020 Review:** The outbreak of Covid-19 dampened the fiscal position, as the region's fiscal deficit reached 58% of GDP in 2020, the highest level in almost 20 years.
- **Revenue projections:** Revenue in the region is poised to improve in 2021, as recovery in commodity prices and tourism activities will support foreign exchange earnings. Also, the region looks to increase tax revenue by introducing e-tax filing system. For example, Kenya, and Uganda have shown improved collection efficiency through simplified tax administrations.
- **Expenditure projections:** We expect increased expenditure this year, in a bid to boost rapid economic recovery.
- With widening fiscal needs and limited finances, a few countries in the region looked to their central banks in 2020 to help fund their crisis spending (the Democratic Republic of Congo, Ghana, Mauritius, Nigeria, South Sudan, Uganda). This trend will likely continue in 2021.
- In the medium to long term, we expect improving exports and fiscal consolidation in major countries like Ghana, Kenya, to help reduce the risk of debt distress.

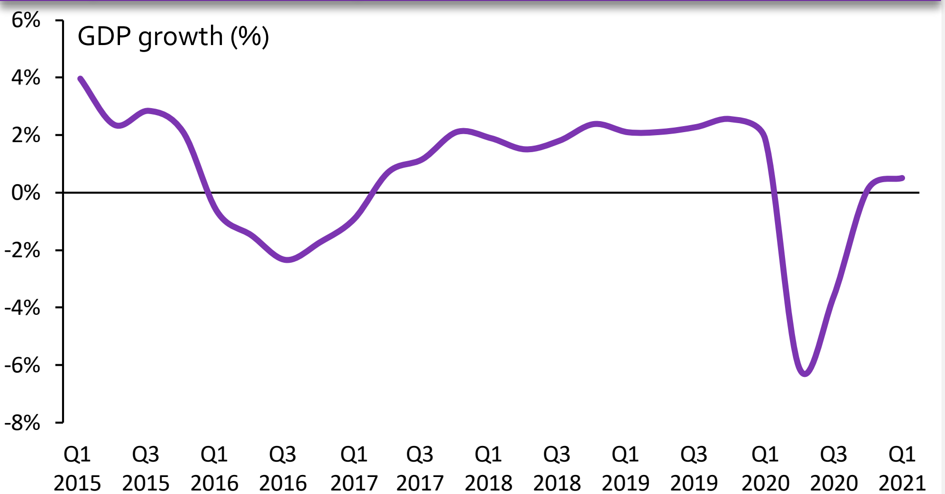
Sources: IMF debt sustainability analysis, Bloomberg, CSL Research

SECTION 2

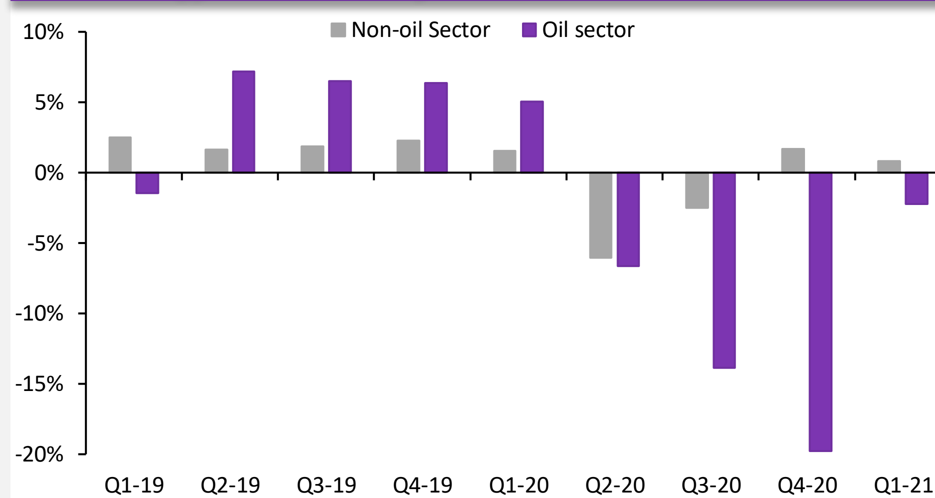
DOMESTIC ECONOMY AND CONSUMER PRICES

FRAGILE ECONOMIC RECOVERY IN Q1 2021

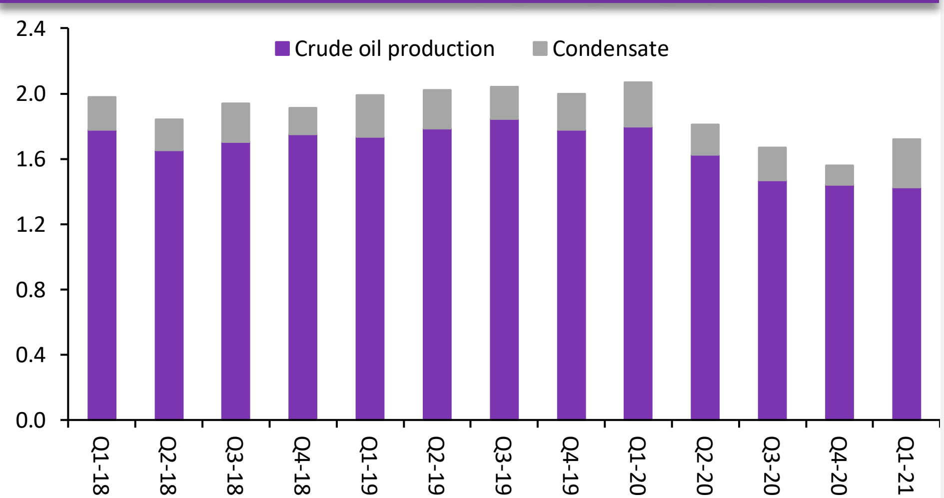
V-shaped economic recovery



Services dragged non-oil sector growth in Q1 2021



Contraction in the Oil sector narrowed, signaling a bright prospect

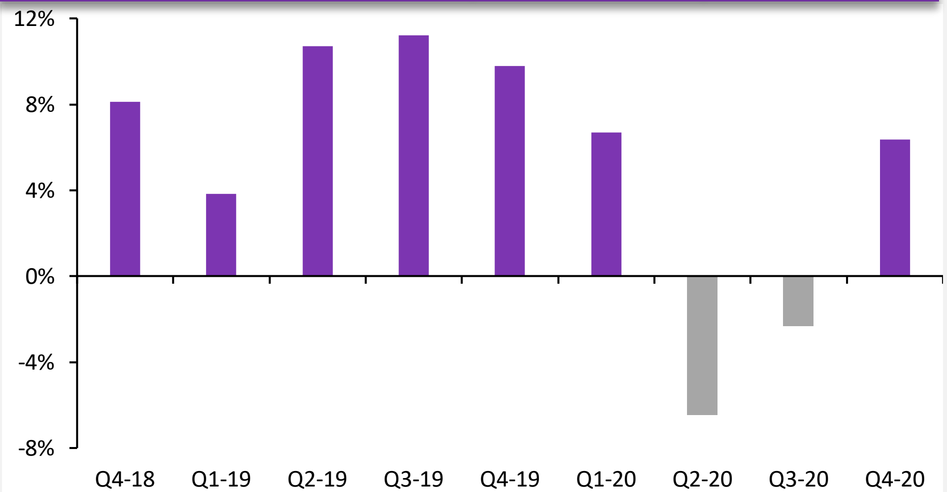


- ❑ Economic recovery continued in Q1 2021, as growth settled at 0.5% (Q4 2020: 0.1%).
- ❑ Although the non-oil sector remains the major catalyst for the positive GDP growth, yet output moderated to +0.8% from +1.7% in Q4 2020. This was mainly due to an uninspiring performance from the services sector (50% of the GDP) which contracted by 0.39% from a positive position of 1.31% in Q4-2020. This reflects the impact of the policy directive from NCC to halt new SIM registrations.
- ❑ Also, cyclicality and the impact of security challenges in the food-producing regions were evident in the Agriculture sector, which expanded, but at a slower pace of 2.28% when compared with 3.42% in Q42020.
- ❑ The oil sector declined, but at a slower pace of 2.2% (Q4 2020: -19.9%), supported by improved crude oil production (including condensate), which settled at 1.72mb/d from 1.56mb/d in the prior quarter.

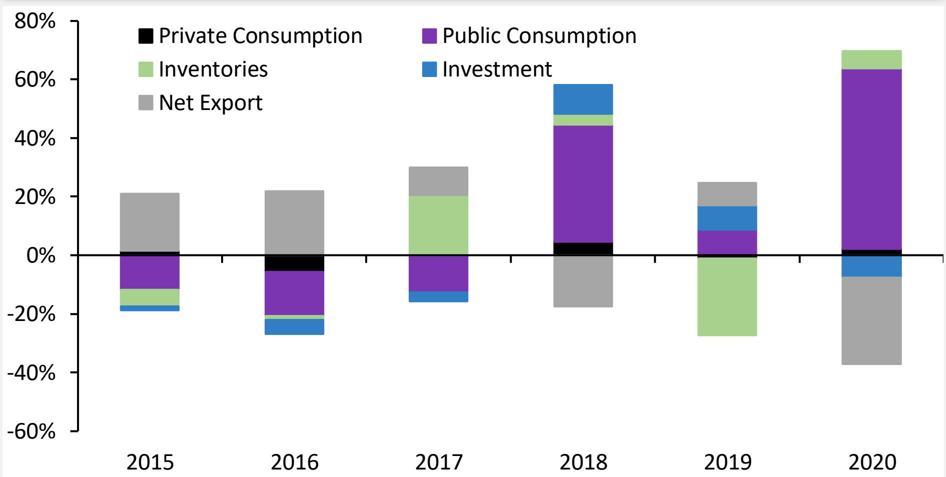
Sources: NBS, OPEC, CSL Research

DEMAND SIDE ANALYSIS: IMPROVING CONSUMPTION TO DRIVE GROWTH IN 2021

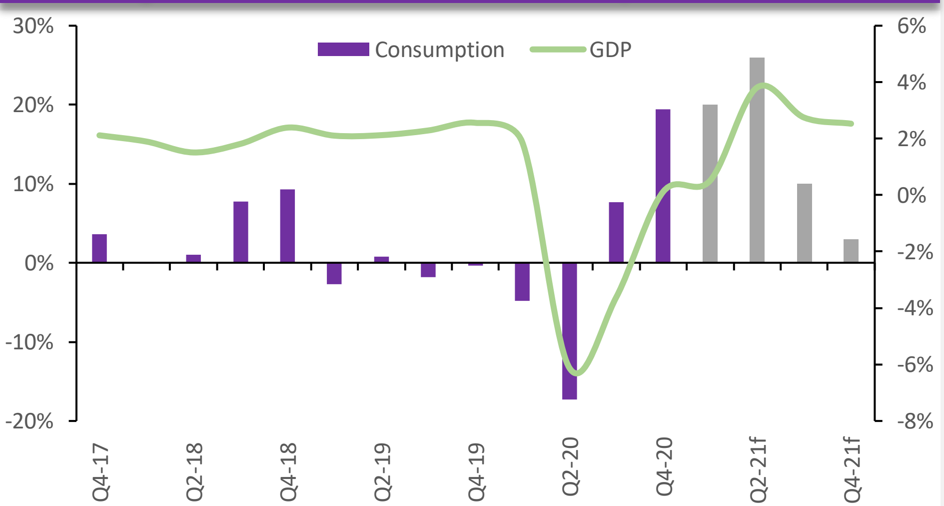
Household income continues to recover, but remains below pre-Covid levels



Fiscal spending increased in 2020 to combat Covid-19



Domestic growth to move in tandem with consumption

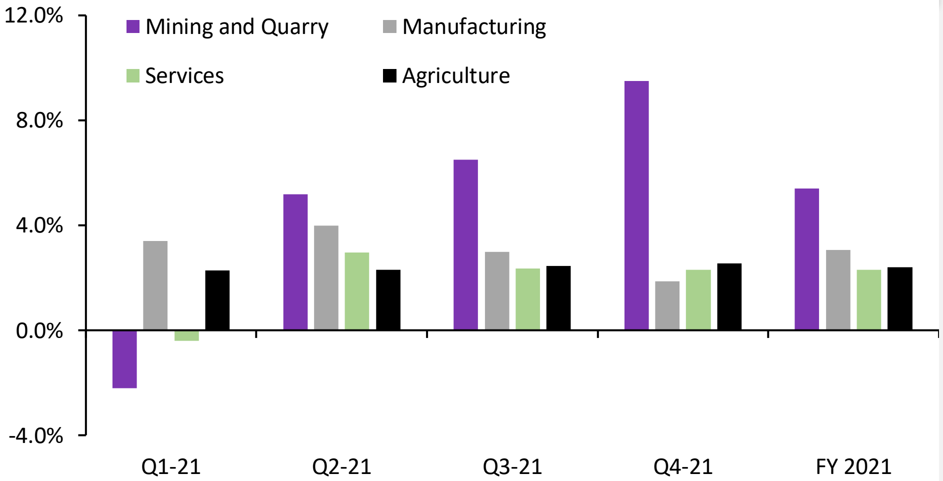


Unemployment soars to record high in 2020

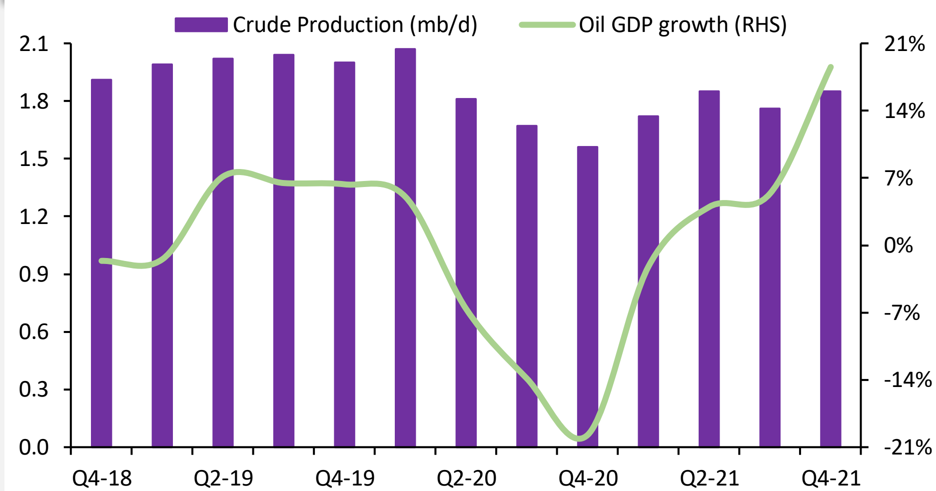
Sources: NBS, CSL Research

More Room for Growth, We Estimate FY 2021 Output Of 2.4%

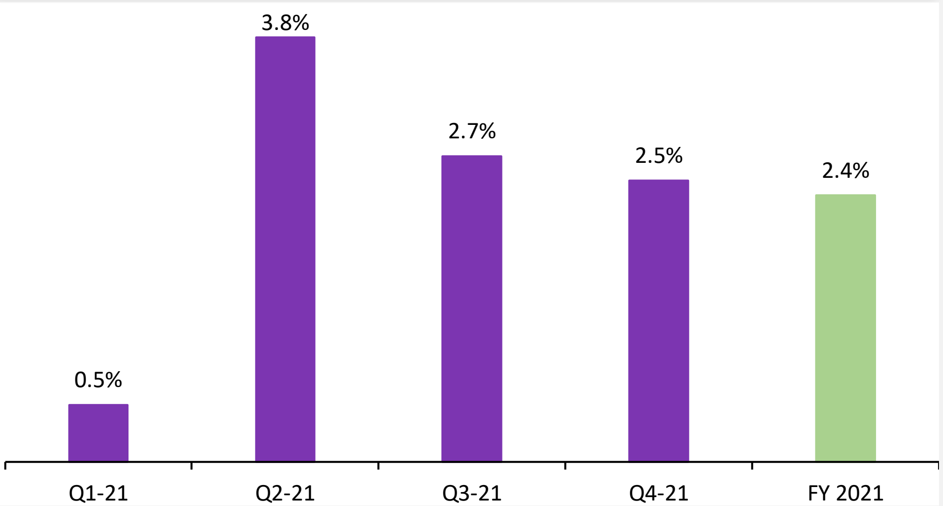
Growth projections across various sectors of the economy



Outlook for oil remains cautiously optimistic



Projected growth for 2021

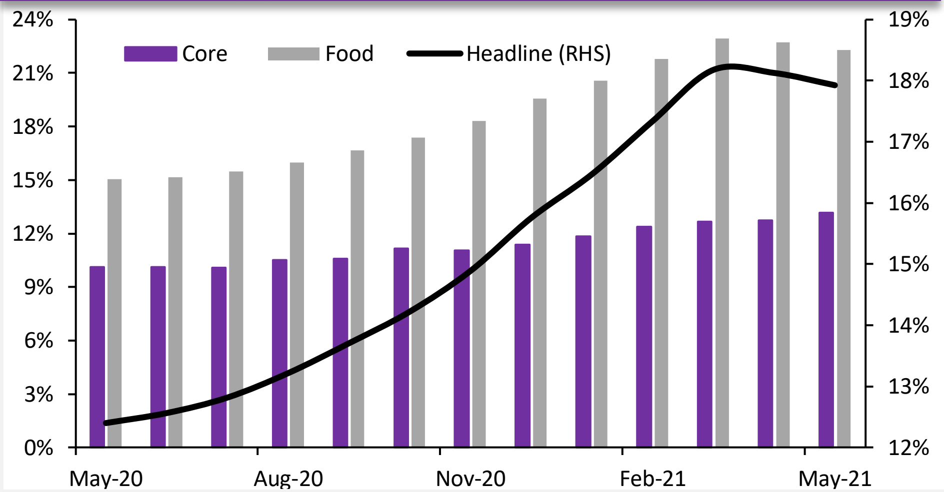


- Normalisation of economic activities and rebound in oil prices to further support recovery. **We project growth to settle at 2.4% in 2021.**
- **Non-oil sector:** We expect growth to accelerate in the non-oil sector, supported by; (1) positive pass-through from low base in 2020, (2) recovery in the services GDP as the NCC has lifted the embargo on SIM registration in the country and (3) resilience of the agriculture sector.
- **Oil sector:** Outlook for oil remains cautiously optimistic. Although oil prices have increased, oil production is unlikely to reach pre-pandemic levels till 2022. We forecast average crude production of 1.8 million barrels a day for the rest of the year.
- Exiting recession could have been an easy task, but fiscal and structural reforms will be required for growth to return to 2015 level of about +6.7%.
- Despite the gradual economic recovery, the 2020 recession is expected to have lasting effects on poor and vulnerable households.
- **Downside risks to our outlook:** Security challenges and crude oil price related shocks.

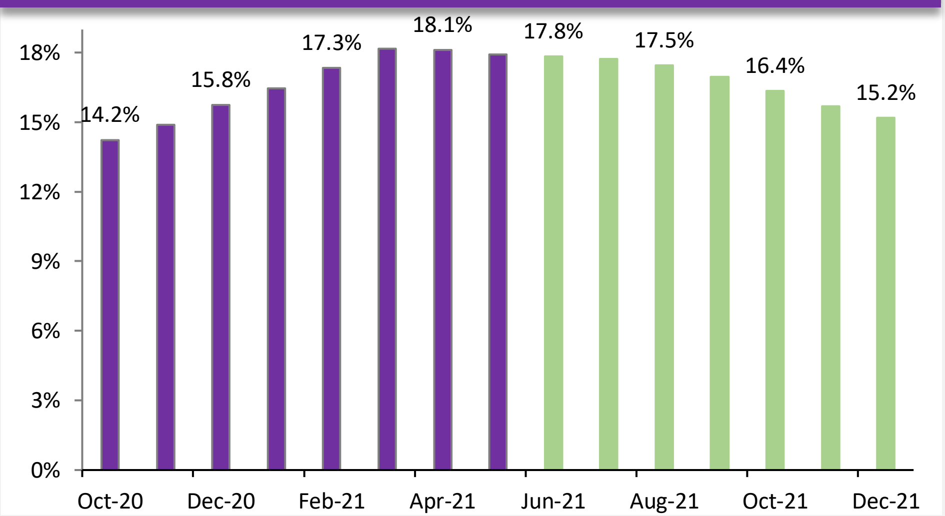
Sources: NBS, CSL Research

INFLATION REACHED AN INFLECTION POINT IN H1 2021

Trend in Inflation (%)



Headline inflation (%)



Sources: NBS, CSL Research

Inflation is H1 2021 was a tail of two halves

- In the first quarter of the year, inflation soared, reaching 18.2% in March (a 4-year high), on the back of exogenous factors like conflict in food-producing regions and policy factors like trade restrictions, exchange rate movement etc.

- The dynamics changed in Q2 2021, as prices dropped, supported by gains from dry season harvest and positive pass-through from a high base. As such, inflation retreated to 17.9% in May.

- The inflationary movement has been in tandem with the food basket of the CPI. The surge in domestic food prices accounted for almost 70% of the rise in inflation over the 12 months.

- Core inflation was elevated, on the back from pressured prices from energy costs and currency devaluation.

Inflation to decline further in H2 2021 due to high base effect

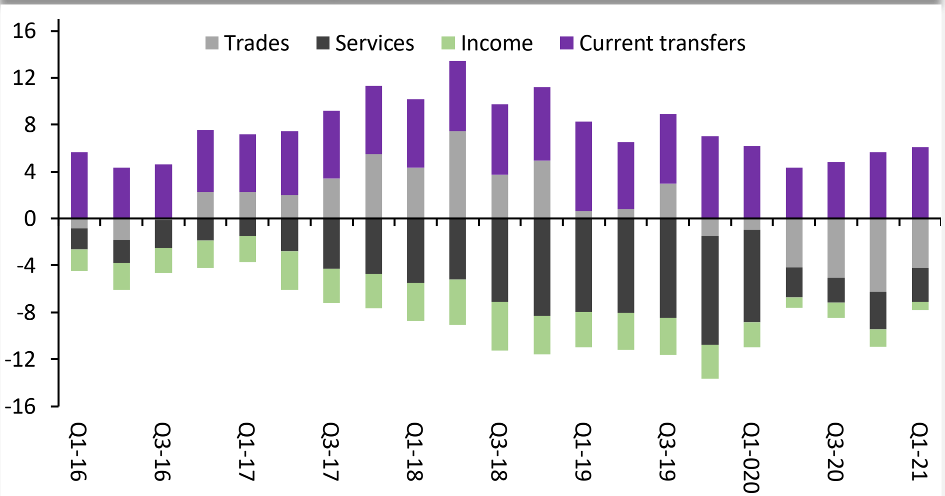
- Over the second half of the year, inflation is projected to further moderate, mainly due to the high base effect from the corresponding period last year.
- Besides base effects, the risk of increasing inflation remains elevated. In our view, food prices will continue to soar, as security challenges continue to threaten agricultural productivity. Furthermore, possible halt in food supply from various agitating groups like the Onion Producers and Marketers Association (OPMAN) and Amalgamated Union of Food Stuff and Cattle Dealers of Nigeria (AFUCDN) remains a major risk factor.
- Risk to core inflation remains tilted to the upside, emanating from possible electricity price hikes and higher PMS prices. We see less currency pressure in H2 2021.
- Overall, we project average inflation rate to moderate to 16.6% in H2 2021 (H1 2021: 17.6%).

Section 3

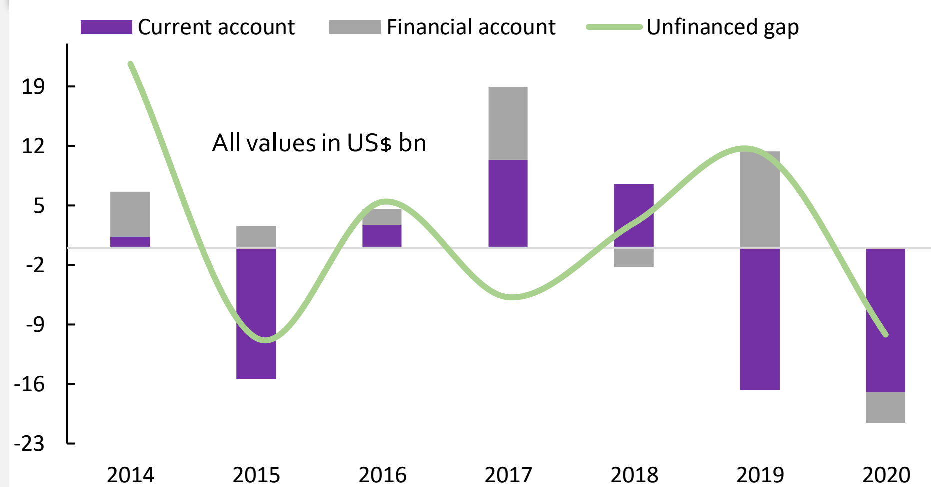
FX and External Sector

CA DEFICIT NARROWS IN Q1 2021, BUT TRADE BALANCE REMAINS WORRISOME

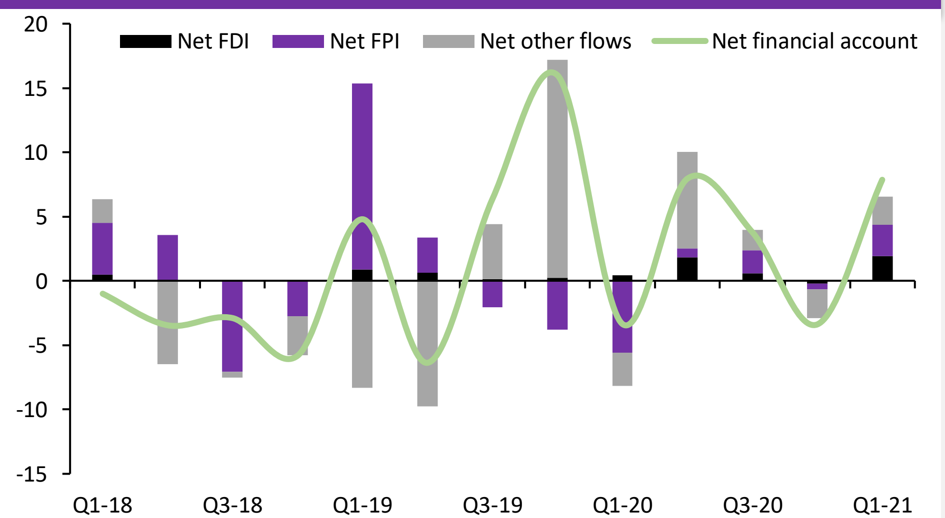
Current account Sub-Components (Us$ bn)



Nigeria's Balance of Payments Gap (US$bn)



Composition of Nigeria's financial account balance (US$bn)

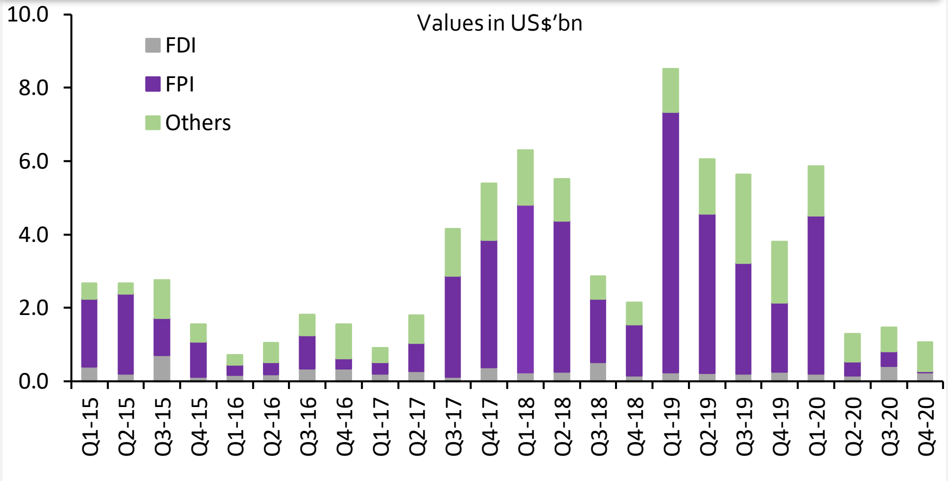


Sources: CBN, CSL Research

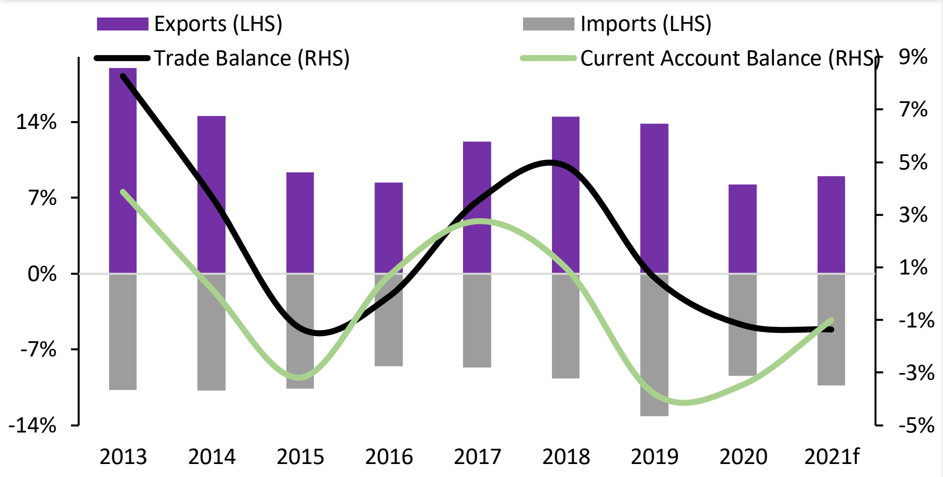
- In Q1 2021, current account deficit moderated to US$1.75bn (1.7% of GDP) from US$5.26(5.0% of GDP) in Q4 2020.
- Export earnings declined by 8.7%q/q. While crude oil price is at a 2-year high of 74.43bbl, the OPEC+ agreement continues to place a cap on oil earnings, as oil production (excluding condensate) settled at 1.4mb/d in Q1.
- On the flip side, foreign outflows reduced, as imports declined by 18.7%q/q. For us, this depicts two things; (1) domestic consumption (c.60% of GDP) is yet to recover to pre-pandemic levels and (2) intensified FX control by the CBN.
- Also, remittances (+5.6%q/q) are gradually recovering, reflecting the improved wellbeing of Nigerians in diaspora and the likely impact of CBN's Naira 4 Dollar Scheme.
- On the financing front, despite the macroeconomic headwinds and regulatory uncertainty, foreign portfolio inflows improved to US$2.4bn from a negative position of US$0.4bn in Q4 2020. This perhaps indicates foreign investors are taking advantage of the carry trade opportunity in the market.

CA DEFICIT TO NARROW ON IMPROVING GLOBAL ECONOMY AND HIGHER CRUDE OIL PRICES

Capital importation fell to pre-IEW levels, but likely to recovery in H2 2021



CA deficit is projected to narrow to 1.2% of GDP in 2021



CA indicators	2019	2020	2021f
Current A/c Surplus/Deficit (US$'bn)	(16,739.5)	(20,312.5)	(4,333.9)
Projected average inflation			17.0%
Estimated GDP deflator	201.9	217.6	230.0
Projected Real GDP (N'm)			71,484,673.6
Projected Nominal GDP (N'm)	144,210,492.1	152,324,070.6	164,414,749.3
Exchange rate	306.3	355.5	410.0
Nominal GDP (US$'bn)	470,741.4	428,526.6	401,011.6
CA as % of GDP	**-3.6%**	**-4.7%**	**-1.2%**

- In 2021, the CA deficit is expected to narrow to 1.2% of GDP, supported by a rebound in oil prices and recovery in the global economy. Crude oil prices have firmed in 2021, currently trading at US$76.51/bbl as of 13 July 2021. The recovery is driven mainly by resurgence in global demand and supply-side factors, especially the OPEC+ production agreements.
- Remittances are expected to recover as rising vaccination rates and effective containment measures strengthen foreign labour markets.
- Also, the re-opening of the borders and the implementation of the African Continental Free-Trade Area agreement (AfCFTA) will likely support non-oil exports.
- To correct this external imbalance, we see a 6%-9% likely devaluation of the NGN by year-end.

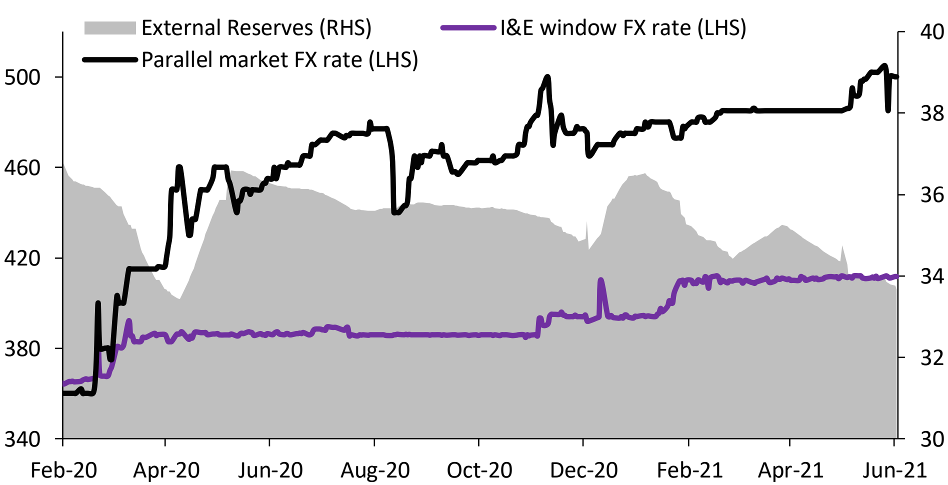
Sources: NBS, CBN, CSL Research

CSL

NGN: CONVERGENCE TAKES CENTRE STAGE

Windows	Participants/use	Current rate	Previous rate (Dec 2020)	Level of liquidity
Official exchange rate	Government transactions, oil revenue estimate & Budgets	c.410	379.0	CBN sells US$50,000 to each bank every month
Investors and Exports Windows (IEW)	Investors, Exporters and all market players(both foreign and domestic	c.410	392-410	Liquidity has averaged US$84.4m in 2021
Retail Secondary Market Intervention Window	Local corporates, mostly manufacturers	390-435	381-425	US$100 - 150m sold by the CBN bi-weekly at the spots and forward markets
BDCs	Open to all	482-500	393-395	CBN sells US$20,000 to each BDC weekly
Parallel market	Open to all and those without access to official windows	485-510	470-485	

IEW rate was stable in H1, while parallel market rate crossed N500/US$

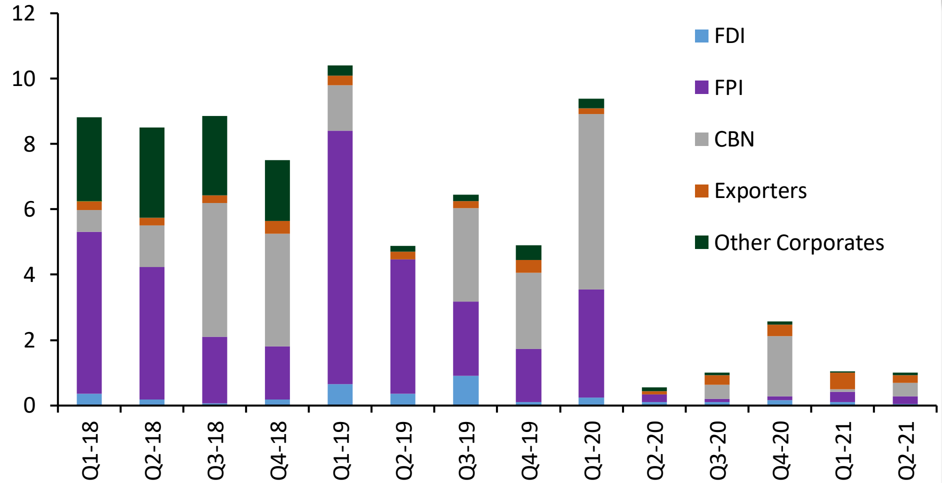


Sources: CBN, Abokifx, CSL Research

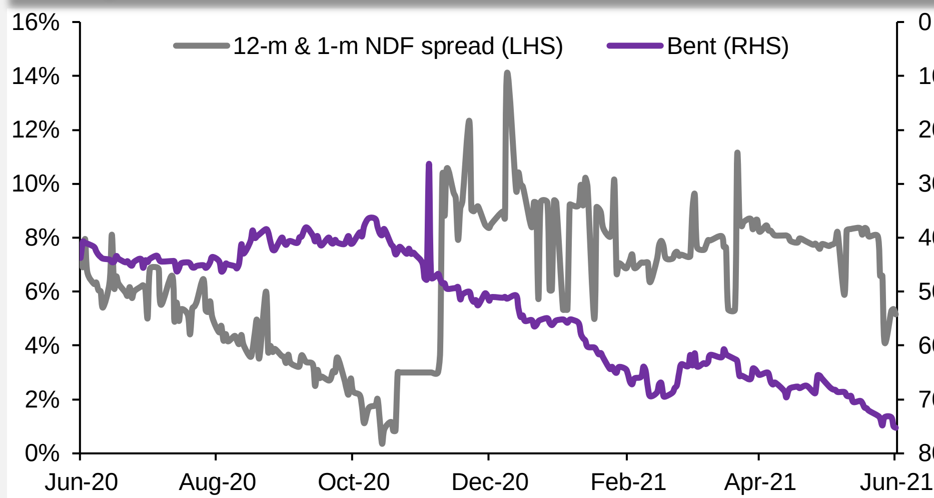
- In the first half of the year, Naira was relatively stable at the I&E window, but the parallel market rate scaled to an all-time high.
- Despite the rebound in oil prices, reserve pared by 5.8%, reflecting increased CBN FX interventions and low impetus for new foreign inflows.
- FPI funds which historically contributed about US$13.14bn on average to the total FX reserve now accounts for about c.US$5.1bn.
- The CBN managed exchange rate pressures in H1 2021 via 3 major administrative measures;
  - FX convergence, by adopting the IEW rate as the official FX rate.
  - Introduction of Naira 4 Dollar Scheme, which offers a N5 incentive for every dollar received as a remittance inflow through licensed international money transfers operators.
  - FX restriction for both sugar and wheat.
- All these measures yielded little results in narrowing the parallel market premium (23%) .

LIQUIDITY ACROSS THE FX STRATA STILL TRAILS PRE-COVID LEVELS

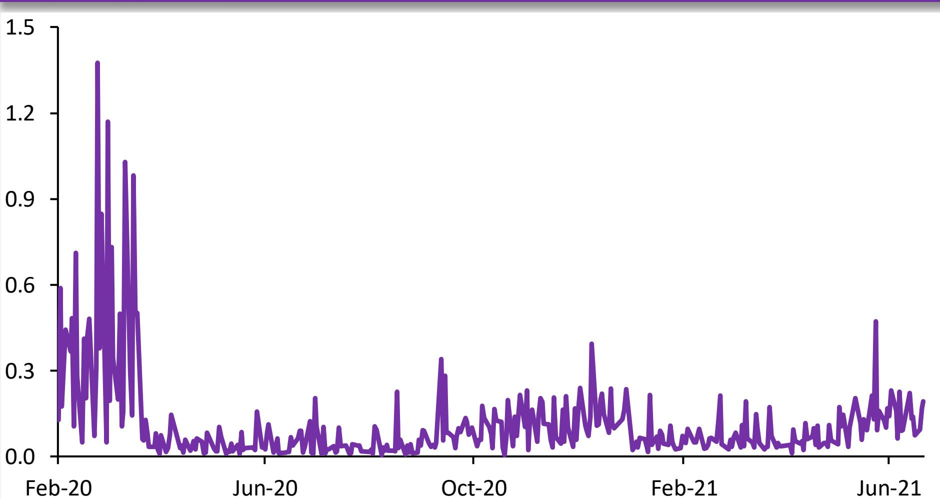
Foreign inflows (US$'bn) remain tepid, trailing pre-pandemic level



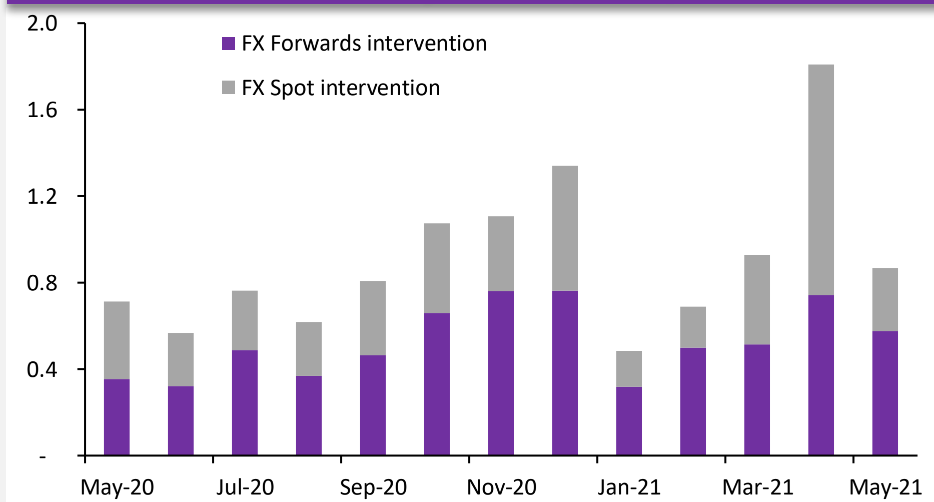
NDF spread and Crude oil



Liquidity (US$'bn) remains low at the IEW



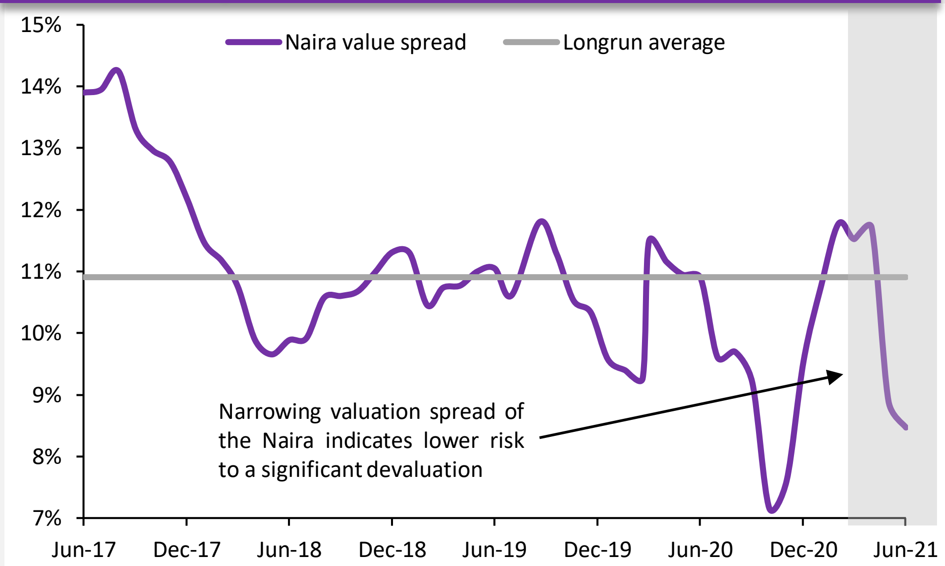
Intervention at the forward and spot market (US$'bn)



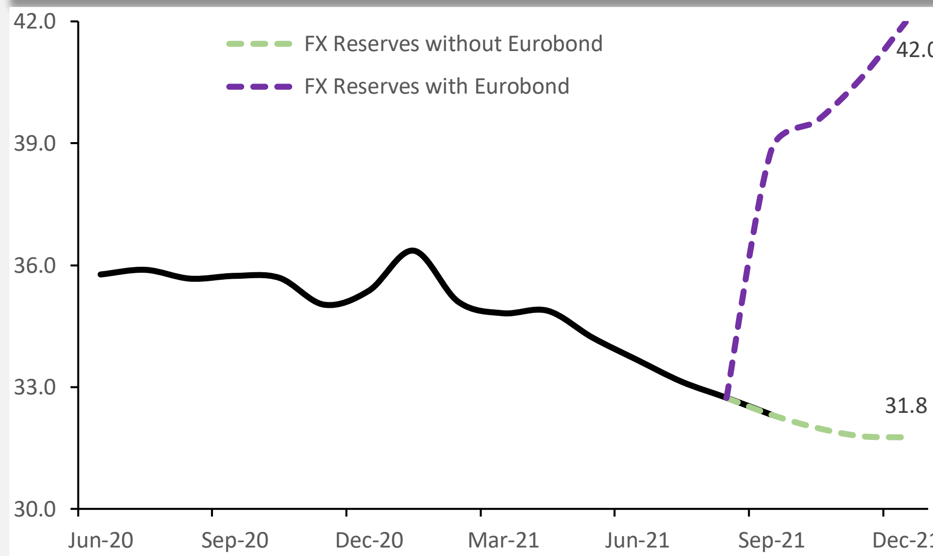
Sources: NBS, CBN, FMDQ, CSL Research

NGN REMAINS OVERVALUED, BUT A LARGE DEVALUATION IS UNLIKELY

Naira valuation spread has narrowed in recent months



FX Reserves (US$'bn)



FX Blended Valuation	Weighting	FX rate
Current IEW rate		411.3
Purchasing power parity	40.0%	464.8
Uncovered Interest Rate Parity	60.0%	436.6
Weighted average		**447.9**
Naira fair value valuation spread		**8.9%**
Over/under valuation		**Overvalued**

- NGN remains overvalued, but the recent tightened spread in Naira valuation and continued rebound in crude oil price is likely to shield a large devaluation.
- Furthermore, we see a strong likelihood of Eurobond issuance in either late Q3 or early Q4. We assume the government will issue between US$3.0-6.0bn.
- With the expected Eurobond inflows, clarity on FX and other administrative tactics adopted by the CBN, we expect foreign investors confidence to improve in Q4 2021.
- The proposed increased SDR allocation by the IMF for its member countries could also provide support for Nigeria's external reserve accretion this year. The expectation is that Nigeria's SDR allocation increase could be closer to US$3bn, which could prompt the government to approach the IMF for further RCF-type financing when the allocations are concluded in Q3.

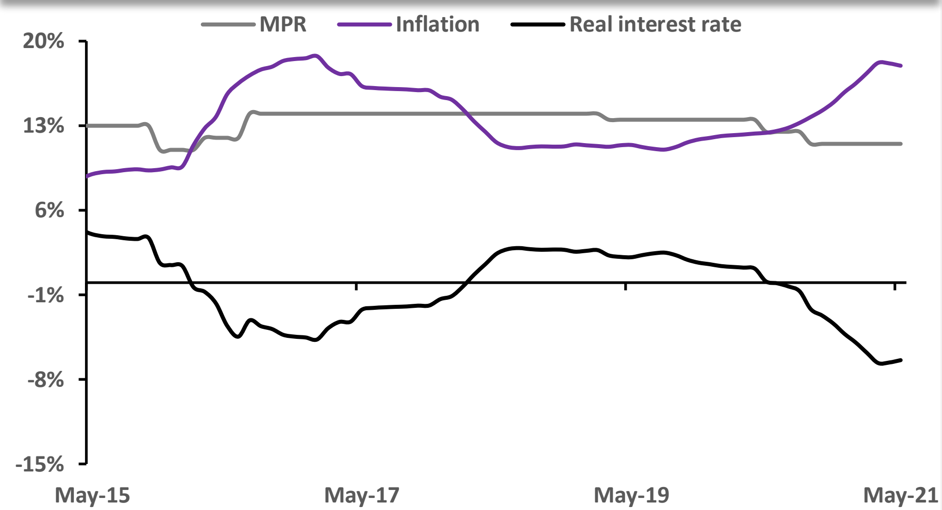
Sources: CSL Research

SECTION 4

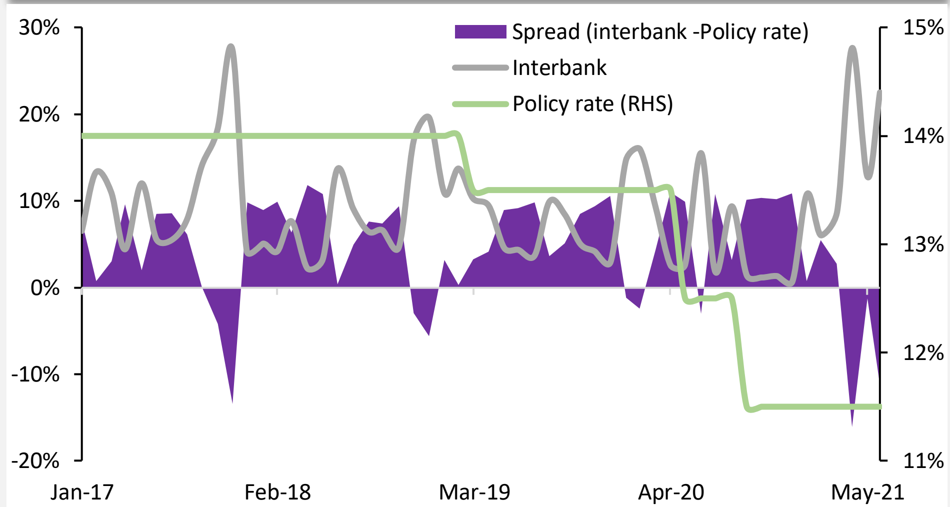
MONETARY POLICY AND FISCAL BALANCE

The CBN to progressively change its policy to a hawkish stance

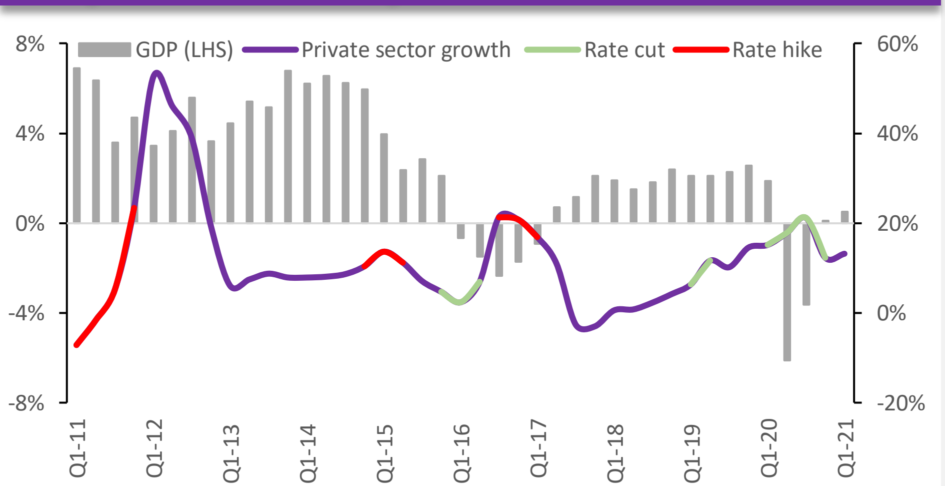
Policy rates and Inflation (%)



Policy rates and interbank rates



GDP growth vs. Private credit growth



- ❑ Over the first half of the year, the MPC held the rate constant at 11.5%. This view seems justified, given the elevated output gap and the poor transmission of rate adjustments to curb inflation.
- ❑ With growth projected to strengthen for the rest of the year and inflation expected to further decline, the CBN might progressively re-direct its policy to a hawkish stance, in favour of exchange rate stability.
- ❑ We see a likely rate hike of 50-100bps in H2.
- ❑ We expect foreign inflows to improve in Q4 2020, supported by (1) less intricate FX regime in Nigeria, following the gradual shift towards convergence, (2) carry trade opportunity that exists In the OMO market, (3) rebound in crude oil prices, (4) improved FX liquidity emanating from likely inflows from Eurobond issue and SDR allocation and (5) recovery in the domestic economy.
- ❑ We expect the CBN to maintain efforts to increase credit to the private sector by sustaining the LDR policy.
- ❑ Finally, we expect the CBN to intensify CRR debits to mop up excess liquidity that might lead to a resurgence in inflationary pressures.

Sources: NBS, CBN, CSL Research

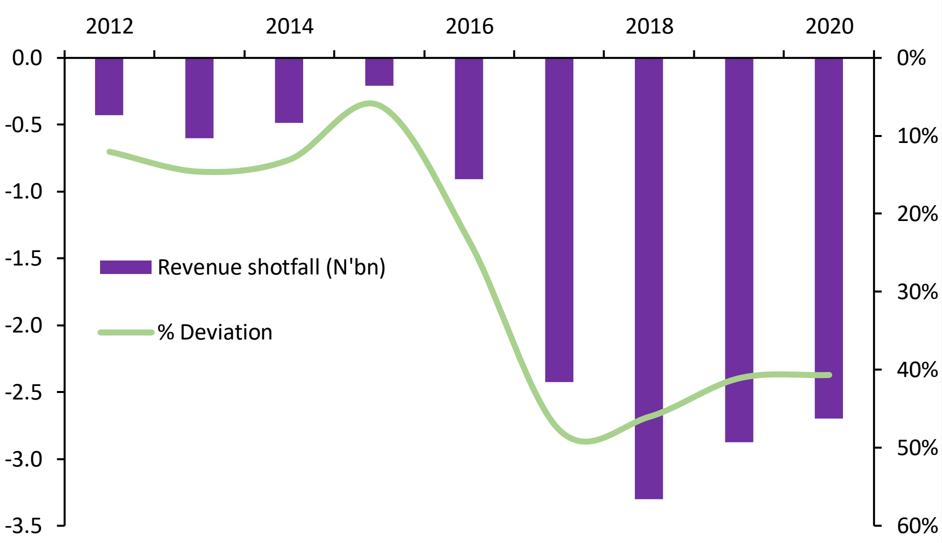
NIGERIA'S FISCAL POSITION, A LOT LIKE DÉJÀ VU

(N'bn)	Jan-May 2021 Budged	Jan-May 2021 Actual	Deviation
Total revenue (including Top 10 GOEs)	**3,327.67**	**1,844.99**	**-44.6%**
Revenue to GOEs	**-562.01**	**0.00**	**-100.0%**
Retained revenue (excluding top 10 GOEs)	**2,765.66**	**1,844.99**	**-33.3%**
Oil	**837.92**	**432.00**	**-48.4%**
Non-oil	**620.39**	**618.76**	**-0.3%**
Corporate Income Tax	284.05	290.90	**2.4%**
FGN Share Customs Revenue	211.78	188.34	**-11.1%**
Value Added Tax (VAT)	99.34	123.85	**24.7%**
Independent revenue	**442.46**	**487.01**	**10.1%**
Other Sources of Financing	**765.55**	**183.37**	**-76.0%**
Total Expenditure	**5,661.00**	**4,857.31**	**-14.2%**
Recurrent non-debt	2,350.82	1,869.95	-20.5%
Debt service (including sinking fund)	1,385.16	1,802.34	30.1%
Capital expenditure (net of GOEs, Project tied loans and statutory transfers)	1,718.81	978.13	-43.1%
Statutory transfers	**206.89**	**206.89**	**0.0%**
Fiscal deficit ex GOEs and project-tied loans	**-2,333.33**	**-3,012.32**	**29.1%**
Deficit/GDP	**-1.6%**	**-2.1%**	
Recurrent Non-Debt Expenditure/Retained Revenue	**85.0%**	**101.4%**	
Debt Service/Retained Revenue	**50.1%**	**97.7%**	
Debt service/GDP	**1.0%**	**1.3%**	
Capex of total Exp	**30.4%**	**20.1%**	
Revenue/GDP	**2.3%**	**1.3%**	
Expenditure/GDP	**4.0%**	**3.4%**	

Legend: GOEs means Government Owed Enterprises

Sources: DMO, CSL Research

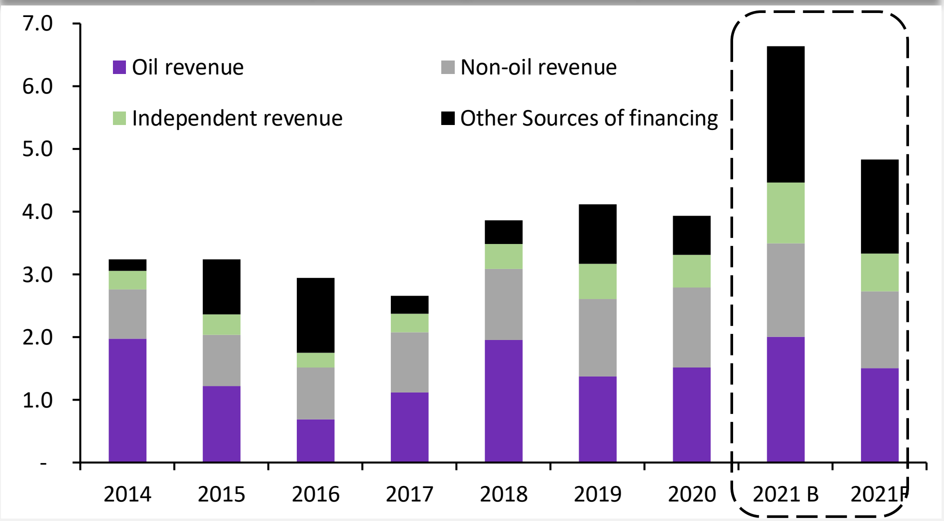
Revenue has significantly underperformed target since 2016



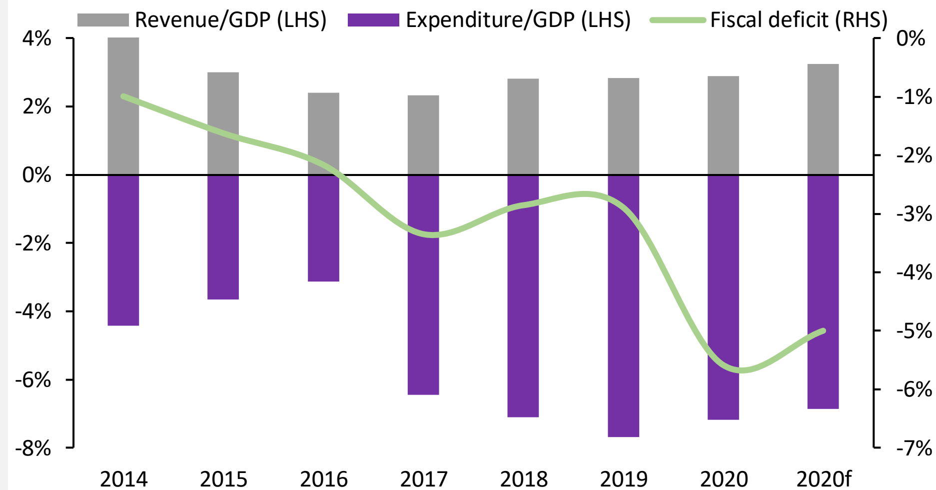
- The fiscal deficit has surpassed the target by an average of c.65% over the last 5 years due to ambitious revenue estimates and volatile crude oil prices.
- The fiscal deficit has more than doubled from 1.0% of GDP in 2014 to about 5.6% in 2020. This is significantly above 3% of GDP as recommended by the Fiscal Responsibility Act (FRA).
- The fiscal slippage in H1 2021 reflects poor performance from oil revenue, as the OPEC+ agreement places a cap on domestic crude oil production. Nevertheless, non-oil nearly outperformed the budgeted estimate.
- Debt servicing to revenue averaging 62% over the last 5 years remains a major concern.

ESSENTIAL SPENDING TO REMAIN CONSTRAINED DUE TO HIGH FISCAL DEFICIT

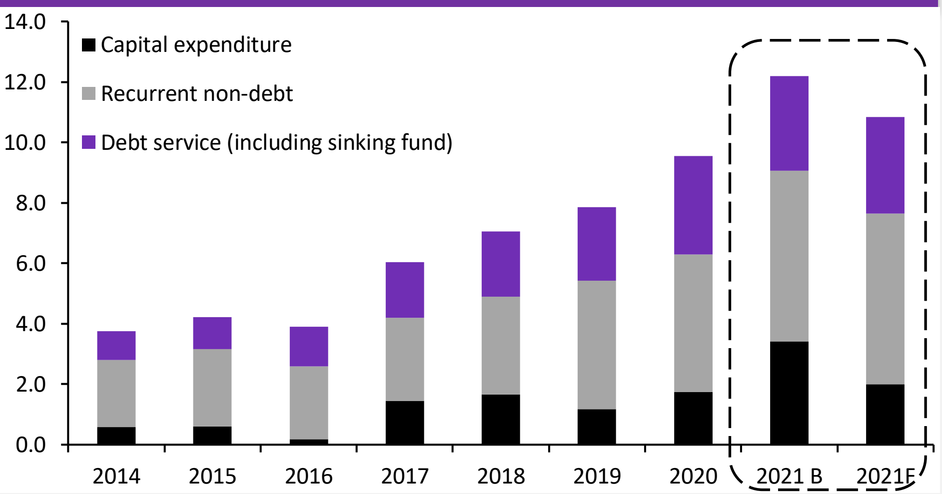
Revenue (N'tn) to underperform budget estimate by 27% in 2021



Fiscal deficit to narrow this year from Covid induced pressure in 2021



High debt servicing (N'tn) cost to limit fiscal space



- Oil revenue is projected to improve in H2 2021, supported by increasing crude oil prices and likely reduction in OPEC production cuts. We expect oil production (including condensate) to average 1.85mb/d from 1.7 in H1.
- Continued recovery in the domestic economy is poised to support the non-oil tax revenue.
- Fiscal deficit to print at 5.0% of GDP in 2021. While this is slightly lower than the 2020 deficit, it is significantly higher than the 5-year average of 3.4%.
- High debt servicing cost at 2.2% of the GDP 2021f will continue to limit fiscal space.
- To finance this deficit, the FGN already raised about 55.8% of the intended domestic borrowing from FGN bonds net NTB issuances. This factors in the newly approved supplementary budget of N982.7bn.
- Following the Senate approval, FGN can issue between US$3.0bn to US$6.0bn in Eurobonds.

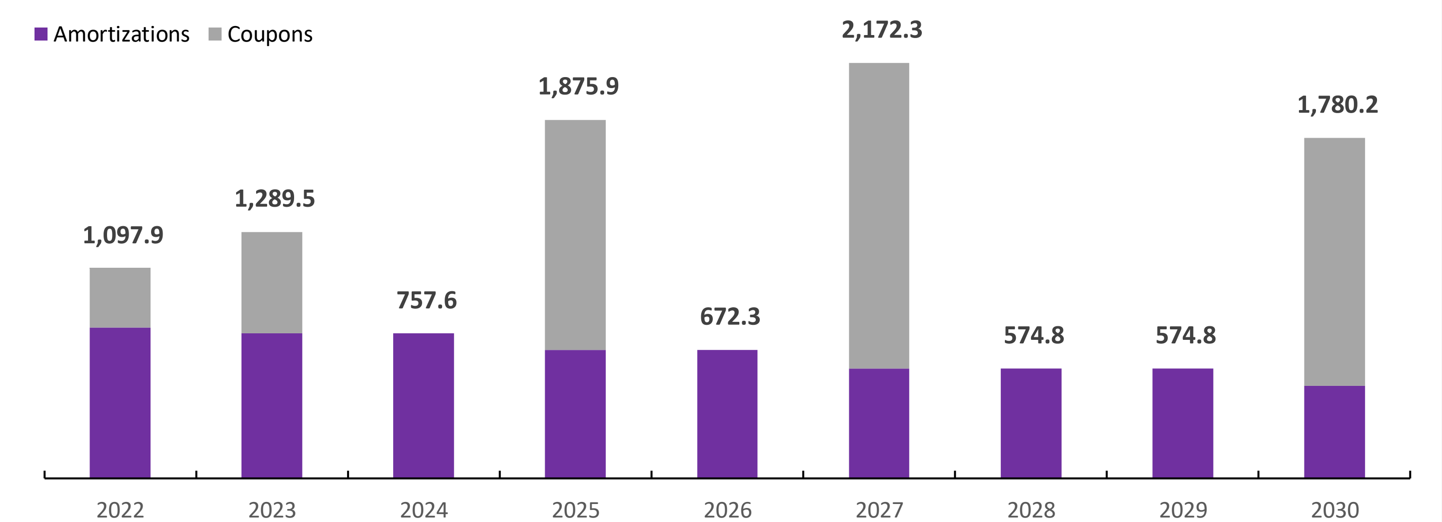
Sources: DMO, CSL Research

EUROBOND ANALYSIS: FUNDAMENTALS SUPPORT ISSUANCE THIS YEAR

NGERIA upcoming coupons and amortizations

Description	Coupon (%)	Outstanding Value ($'mm)	Total coupon	2022	2023	2024	2025	2026	2027	2028	2029	2030
6.75 JAN 28, 2021PT	6.75%	500.00	33.8									
5.625 27-JUN-2022	5.63%	300.00	16.9	308.4								
6.375 JUL 12, 2023PT	6.38%	500.00	31.9	31.9	531.9							
7.625 21-NOV-2025	7.63%	1,118.35	85.3	85.3	85.3	85.3	1,203.63					
6.50 NOV 28, 2027	6.50%	1,500.00	97.5	97.5	97.5	97.5	97.5	97.5	1,597.50			
7.143 FEB 23, 2030	7.14%	1,250.00	89.3	89.3	89.3	89.3	89.3	89.3	89.3	89.3	89.3	1,294.64
8.747 JAN 21, 2031	8.75%	1,000.00	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5
7.875 16-FEB-2032	7.88%	1,500.00	118.1	118.1	118.1	118.1	118.1	118.1	118.1	118.1	118.1	118.1
7.696 FEB 23, 2038	7.70%	1,250.00	96.2	96.2	96.2	96.2	96.2	96.2	96.2	96.2	96.2	96.2
7.625 NOV 28, 2047	7.63%	1,500.00	114.4	114.4	114.4	114.4	114.4	114.4	114.4	114.4	114.4	114.4
9.248 JAN 21, 2049	9.25%	750.00	69.4	69.4	69.4	69.4	69.4	69.4	69.4	69.4	69.4	69.4
		Total debt servicing		1,097.9	1,289.5	757.6	1,875.9	672.3	2,172.3	574.8	574.8	1,780.2

Eurobond servicing (US$'m) is set to remain moderate over the coming years



Sources: DMO, Bloomberg, CSL Research

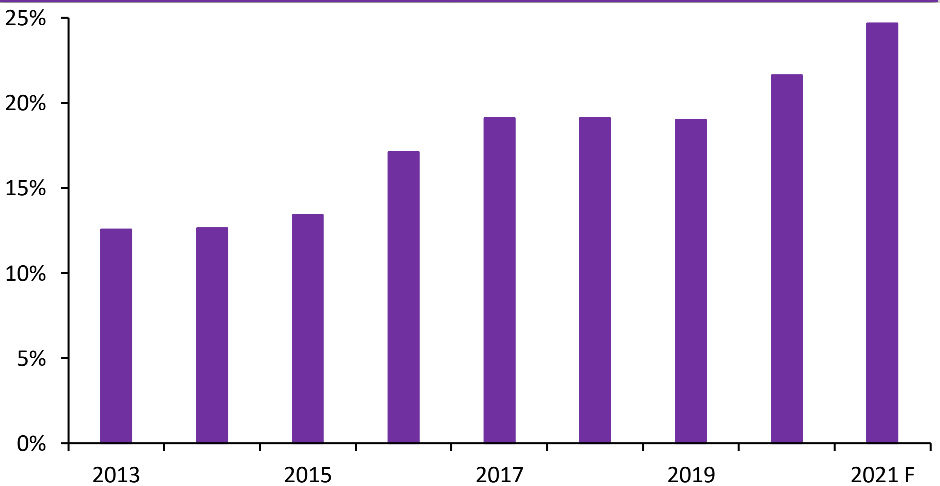
MODERATE RISK OF DISTRESS DESPITE RISING DEBT LEVEL

Public debt burden substantially higher than DMO's estimate

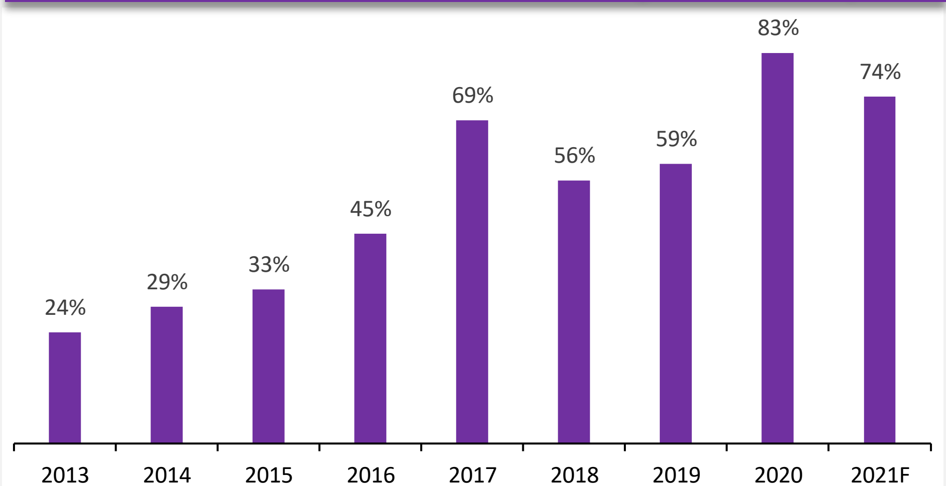
	Debt type	Amount (N'bn)	Amount (US$'bn)	% of GDP
DMO	Domestic debt	20,636.9	54.4	14.5%
	External debt	12,470.4	32.9	8.7%
	Total	33,107.3	87.2	23.2%
Non-DMO	Estimated AMCON debt	4,400.0	11.6	3.1%
	Net liabilities to CBN	8,559.5	22.6	6.0%
	Claims on state and local government by CBN	610.3	1.6	0.4%
	Estimated power sector tariff shortfall	2,180.0	5.7	1.5%
	Total	15,749.8	41.5	11.0%
Total public debt (As of Q1 2021)		**48,857.03**	**128.74**	**34.2%**

- The country still maintains a moderate risk of debt distress due to low stock of foreign currency denominated debts, which has masked the impact of exchange rate shocks.
- Nonetheless, high interest payments will continue to absorb a significant portion of federal government revenues, making the low debt-to-GDP ratio highly vulnerable to shocks.
- Nigeria's total public debt (DMO and non-DMO) is projected to reach 35.5% of GDP in 2021 from 35.0% in 2020. This remains lower than most SSA peers - Ghana (76.7% of GDP) and Kenya (66.5% of GDP) and below 40% set by the DMO.

DMO debt as a % of GDP to rise to 27% in 2021



Debt service/ revenue remains above historic average but below last year



Sources: DMO, CBN, AMCON, world Bank, CSL Research

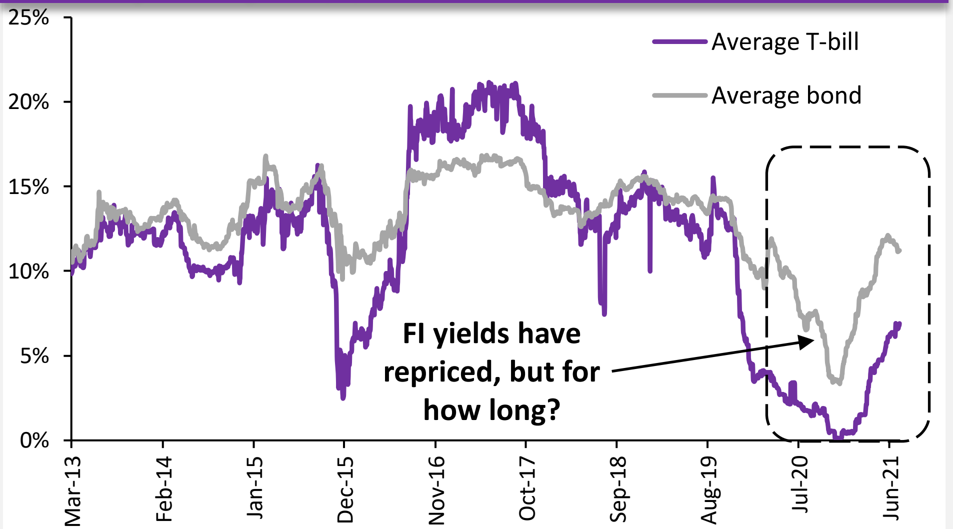
CSL

Section 5

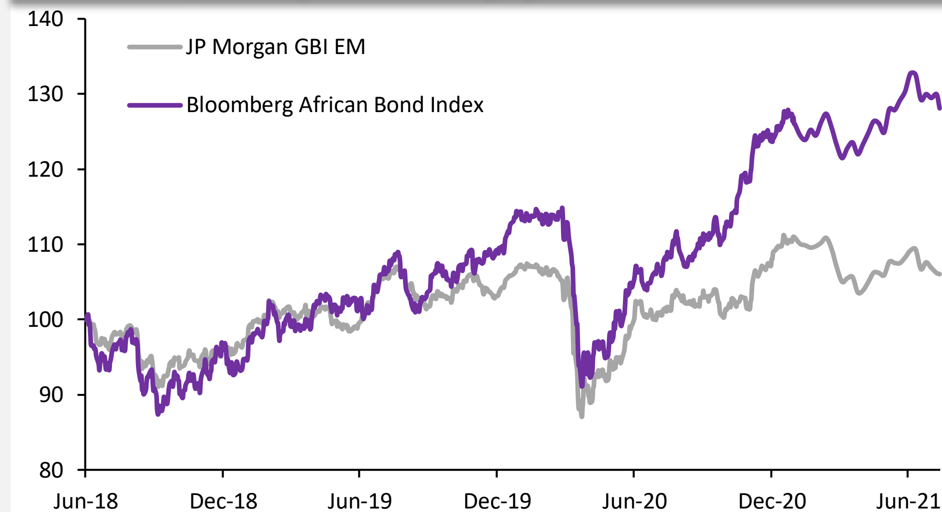
Fixed income review and outlook

FIXED INCOME YIELDS HAVE RECOVERED FROM LAST YEAR'S LOWS

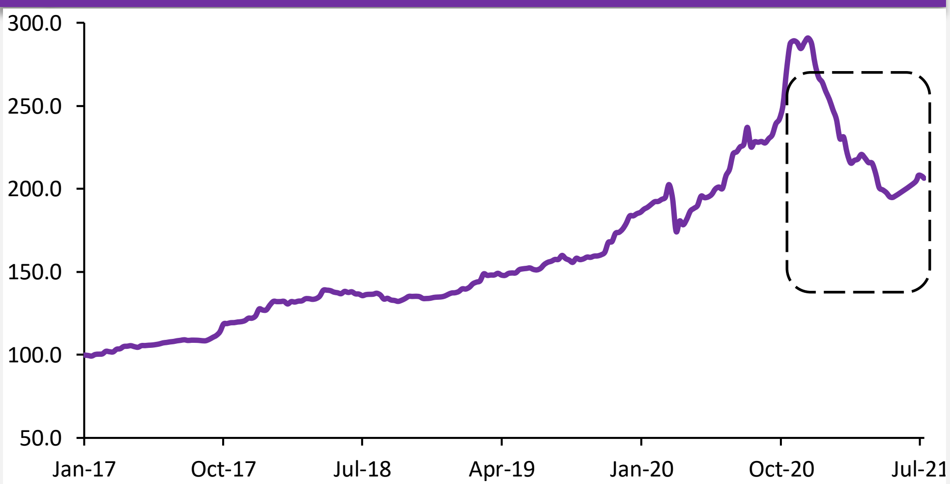
Secondary market yields (%)



Local currency sovereign bonds: Emerging vs African markets



Nigeria's bond market returned -22.8% in H1

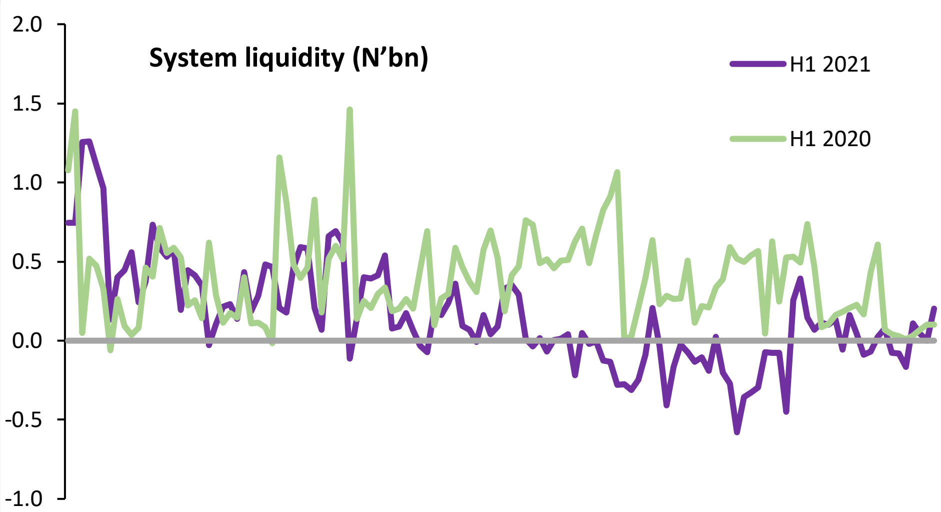


- In 2020, bond yields dropped to a record low, owing to the dovish stance from the CBN and excess liquidity in the financial system.
- The dynamics changed in H1 2021, as the market turned bearish, owing to investors' concern of excessively low yields. As such, the S&P/FMDQ bond index declined by 22.8%
- Another reason for the bearish market performance is due to weak activity level, emanating from low participation from institutional investors.
- Also, the system was devoid of funding, with estimated system liquidity maintaining a lower balance (H1 2020: average: -N156.45bn vs H1 2020 N401.17bn). The increased market participation at the CBN's Standing Lending Facility (SLF) window at N9.07tn, 2.7x higher than H1 2020 indicates the depressed level of liquidity in the system.
- Yields compressed in late June and July. Is this a signal to an inflection point in the market?

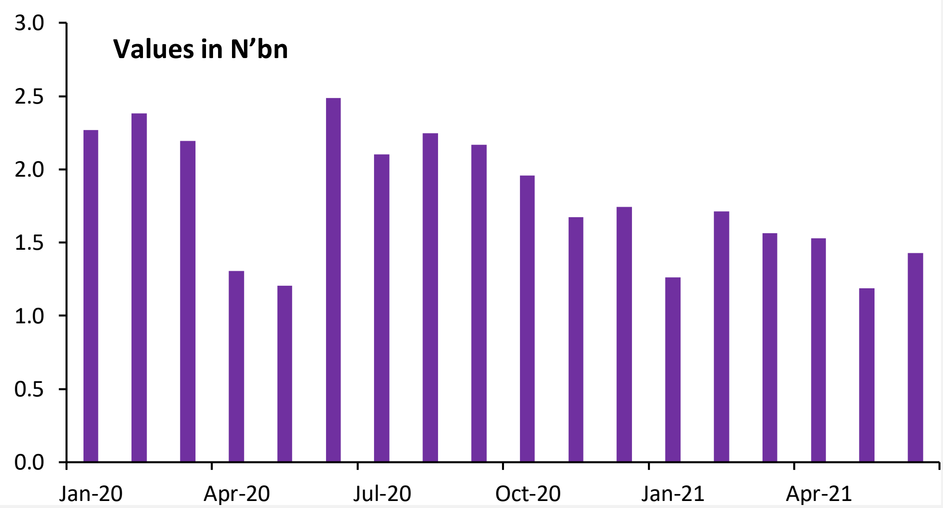
Sources: Bloomberg, FMDQ, CSL Research

Market participation waned in H1 2021, as liquidity thinned out

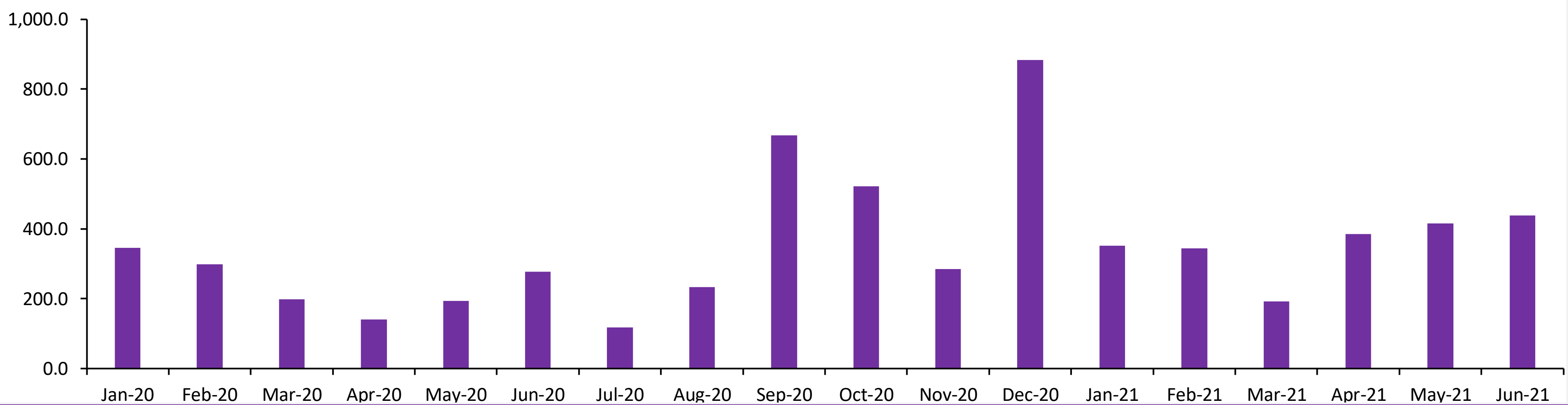
System liquidity settled in the negative terrain in H1 2021



Bond participation declined due to illiquidity and higher yield expectations



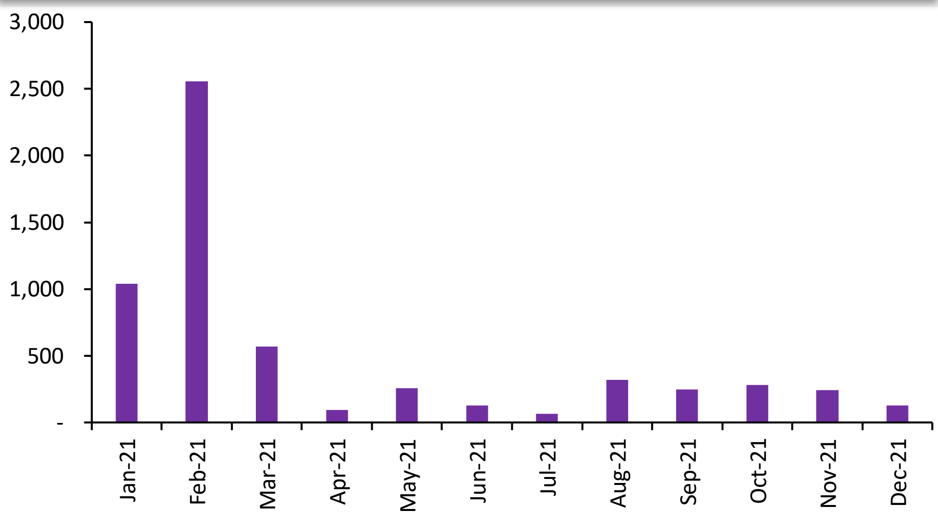
NTB secondary market participation (N'm)



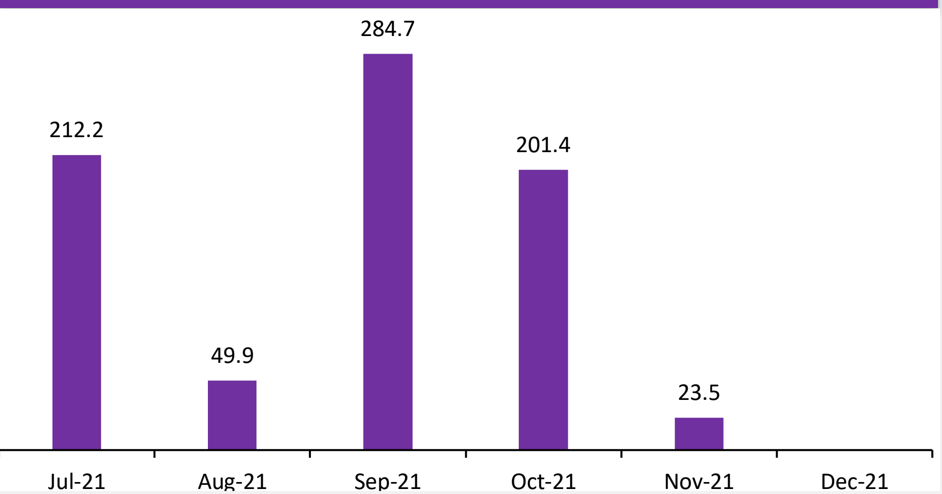
Sources: FMDQ, CSL Research

FIXED INCOME YIELD; NOT AT AN INFLECTION POINT YET

OMO maturities (US$'bn) are expected to drop significantly in H2



Bond coupon payments (N'bn) are significantly low in Q2 2021



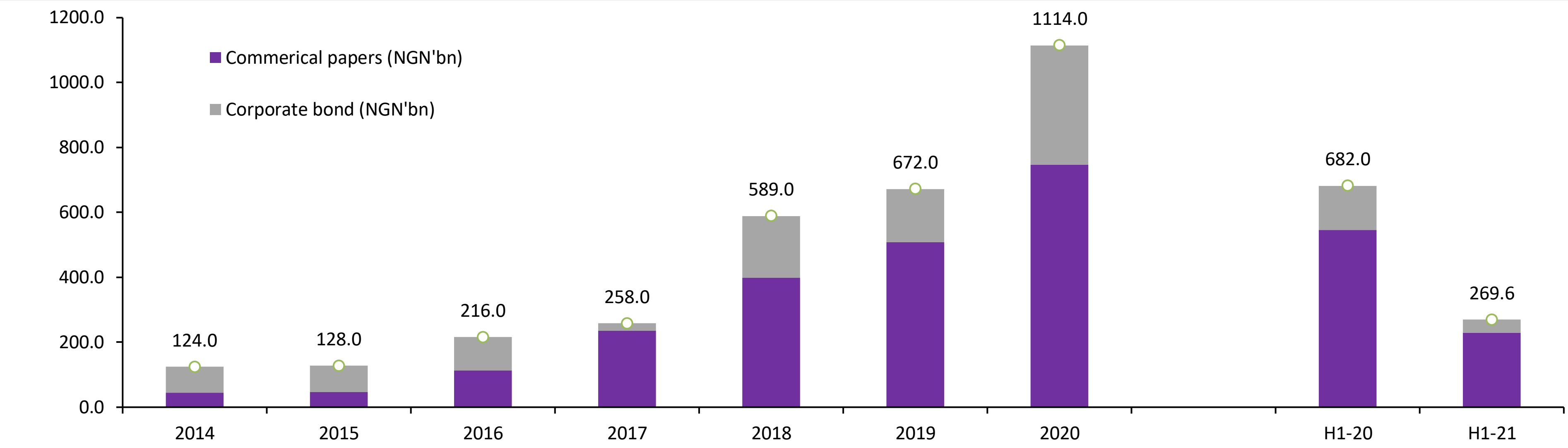
Breakdown of 2021 domestic borrowings	N'bn
2021 domestic borrowings	2,340.0
supplementary budget	982.0
Total proposed borrowings	3,322.0
Amount issued in H1	
Bonds (including non-competitive bids)	1,415.0
NTB net issuance	438.4
Total amount issued	1,853.4
% amount issued in H1	79.2%
% amount issued in H1 (ex supplementary budget)	55.8%

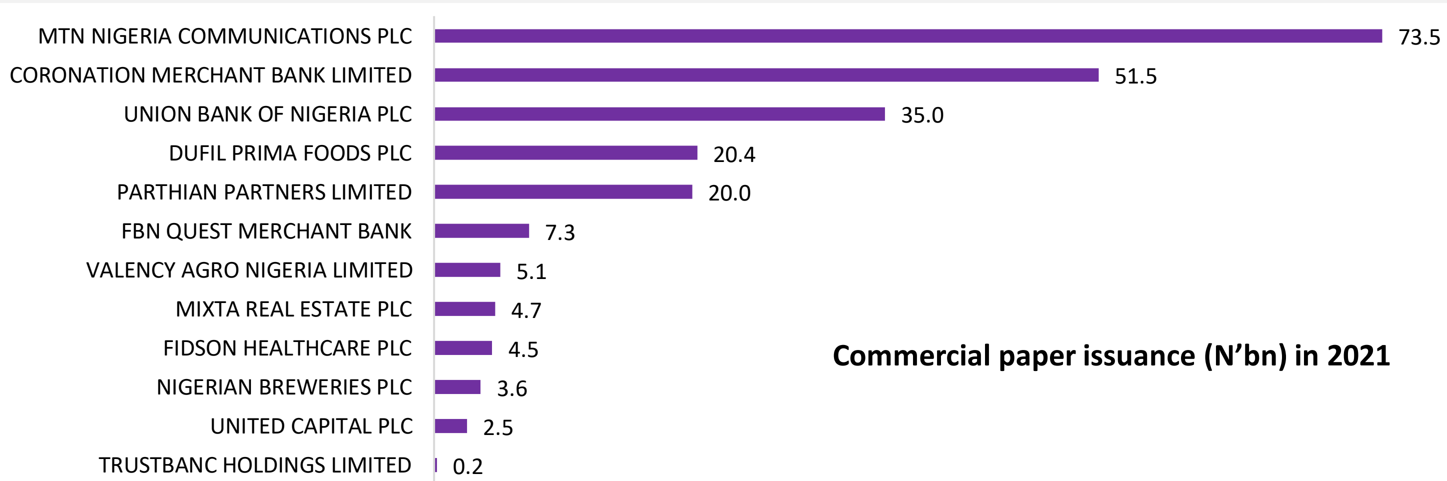
- Maturities and coupon payments across all instruments are estimated at N1.65tn in July 2021. This likely explains the recent decline in average bond yields by c.20bps as of 9 July 2021.
- We do not believe this is an inflection point for the market. To validate this claim, the DMO has net-issued c.N1.85trn in H1 2021, which is about 79% of its planned domestic borrowing which implies domestic supply will be thinner in H2 2021.
- However, adjusting for the recently approved supplementary budget (N982bn), and assuming all the deficit will be sourced from the domestic market, then net issuance so far this year will be only 56% of total planned borrowing.
- From the CBN point of view, higher oil prices have not translated into increased inflows, since the economy is still capped at 1.5mb/d oil production from the OPEC+ agreement. It then leaves OMO as the only viable option for attracting the badly needed FX safe for a Eurobond issuance. Hence, bias is for MPC to turn hawkish in H2 2021 especially in the face of two consecutive positive GDP growth quarters.
- As such, these factors will likely drive investors to demand for higher rates at auctions, which will support secondary market yields to soar.

Sources: DMO, CBN, FMDQ, CSL Research

CORPORATE DEBT ISSUANCES WANED IN H1 2021 DUE TO HIGHER RATES

Corporate debt issuances (ex-private placement and green bond)





- Corporate debt issuances decline significantly in H1 2021, due to higher borrowing rates and low liquidity.
- The dynamics are unlikely to change in H2, as yields will likely remain elevated.

Sources: DMO, FMDQ, CSL Research

ECONOMIC TABLES (TREND & FORECAST)

	2017	2018	2019	2020	2021E
Activity					
Real GDP (% y/y)	0.8	1.9	2.3	(1.9)	2.4
Private consumption (% y/y)	(0.4)	4.6	(1.1)	0.8	1.5
Government consumption (% y/y)	(12.4)	39.9	8.8	61.6	25.6
Oil production (million b/d year-end)	1.9	1.9	2.0	1.8	1.8
Nominal GDP (N'bn)	113,711.6	127,736.8	144,210.5	152,324.0	164,414.7
Nominal GDP (US$'bn)	375.7	398.2	448.1	401.9	401.0
Real GDP (N'bn)	68,491.0	69,799.9	71,387.8	70,014.0	71,484.7
Fiscal balance (% of GDP)					
Fiscal deficit	(3.3)	(2.9)	(2.9)	(4.3)	(5.0)
Revenue	2.3	3.0	2.9	3.6	3.0
Expenditure	(5.7)	(5.9)	(5.7)	(9.2)	(7.5)
DMO debt	25.3	28.4	19.9	21.6	0.3
Debt servicing	(1.6)	(1.7)	(1.7)	(3.0)	(2.2)
Debt Service/Retained Revenue	68.6	55.9	59.4	83.4	73.6
External Balance					
Exports (US$'bn)	45.8	61.2	65.0	35.9	42.4
Imports (US$'bn)	(31.3)	(43.0)	(62.1)	(52.4)	(37.8)
Trade balance (% of GDP)	3.5	4.2	1.5	(4.8)	(1.3)
Current account balance (US$' bn)	10.4	3.9	(16.7)	(20.3)	(4.3)
Current account balance (% of GDP)	3.0	1.5	(3.5)	(4.7)	(1.1)
Net FDI (US$'bn)	2.2	0.6	1.9	2.7	1.4
Prices					
CPI (average % y/y)	16.5	12.1	11.4	13.2	17.1
CPI (year-end % y/y)	15.4	11.4	12.0	15.8	15.2
Interest & Exchange Rates					
Monetary policy rate (MPR), % year-end	14.0	14.0	13.5	11.5	12.0
Credit to the private sector (N'bn)	22,290.7	22,708.2	26,636.6	30,738.7	31,691.6
Credit to the private sector (% y/y)	1.4	1.9	17.3	15.4	3.1
Official exchange rate, (N/US$)	306.0	307.0	307.0	380.0	410.0
I&E exchange rate (N/US$)	360.3	364.0	364.5	395.0	410.0

Sources: CBN, NBS, CSL Research

CONTACT

GLORIA FADIPE
HEAD OF RESEARCH
BANKS
gloria.fadipe@fcmb.com

AYODEJI AJILORE
RESEARCH ANALYST
FMCGS & BREWERS
ayodeji.ajilore@fcmb.com

OLUWASESAN ADEYEYE
RESEARCH ANALYST
INDUSTRIALS
oluwasesan.adeyeye@fcmb.com

OLAOLU BOBOYE
ECONOMIST
SUB-SAHARAN AFRICA
Olaolu.boboye@fcmb.com

ABIODUN FAGBULU
CHIEF EXECUTIVE OFFICER
Abiodun.fagbulu@fcmb.com

DISCLAIMER

Important Risk Warnings and Disclaimers

CSL STOCKBROKERS LIMITED ("CSLS") is regulated by the Securities and Exchange Commission, Nigeria. CSLS is a member of the Nigerian Stock Exchange. CSL Capital (UK) Ltd (Firm Reference Number: 913994, Registered Number: 11818051), trading in the name of 'CSL Stockbrokers' for its activities, is authorised by the Financial Conduct Authority (FCA).

Both CSLS and CSL Capital (UK) Ltd are members of the FCMB Group ("the Group") of Nigeria, a group of companies which also includes First City Monument Bank Ltd.

RELIANCE ON THIS PUBLICATION FOR THE PURPOSE OF ENGAGING IN ANY INVESTMENT ACTIVITY MAY EXPOSE YOUTO A SIGNIFICANT RISK OF LOSS. By receiving this document, you will not be deemed a client or provided with the protections afforded to clients of CSLS and CSL Capital (UK) Ltd. When distributing this document, CSLS, or any member of the Group is not acting for any recipient of this document and will not be responsible for providing advice to any recipient in relation to this document. Accordingly, CSLS or any member of the Group will not be responsible to any recipient for providing the protections afforded to its clients.

If you are in the UK, you are a person to whom either Articles 19 or 49 of the Financial Services and Markets 2000 (Financial Promotion) Order 2005 apply or a person to whom this communication may otherwise be lawfully made.

In the United Kingdom, this document is available only to such persons described above and persons of any other description should not rely on this document. Transmission of this document to any other person in the United Kingdom is unauthorized and may contravene the Financial Services and Markets Act 2000 (FSMA). If you are not such a person or if the distribution of this document is otherwise unlawful where you are, you are required to return the document immediately to CSLS. This document is not intended for Retail Clients in the UK.

This document is not an offer to buy or sell or to solicit an offer to buy or sell any securities. This document does not provide individually tailored investment advice. It has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The appropriateness of a particular investment will depend on an investor's individual circumstances and objectives. The investments and shares referred to in this document may not be suitable for all investors.

CSLS or any other member of the Group may effect transactions in shares mentioned herein and may take proprietary trading positions in those shares, and may receive remuneration for the publication of its research and for other services. Accordingly, this document may not be considered as objective or impartial. Additionally, information may be available to CSLS, or the Group, which is not reflected in this material. Further information on CSLS' policy regarding potential conflicts of interest in the context of investment research and CSLS' policy on disclosure and conflicts in general are available on request.

This document is based on publicly available information obtained from sources which CSLS believes are reliable, but which it has not independently verified. Neither CSLS, or their advisors, directors or employees make any guarantee, representation or warranty as to the accuracy, reasonableness or completeness of this information and neither CSLS or their advisors, directors or employees accepts any responsibility or liability whatsoever (in negligence or otherwise) for any loss howsoever arising from any use of this document or its contents or otherwise arising in connection with this document. The opinions contained in this document are subject to change without notice and are not to be relied upon and should not be used in substitution for the exercise of independent judgment.

DISCLAIMER (2)

Past performance is not a guarantee of future performance. Investments may go down in value as well as up and you may not get back the full amount invested. Where an investment is denominated in a currency other than the local currency of the recipient of the research report, changes in the exchange rates may have an adverse effect on the value, price or income of that investment. In case of an investment for which there is no recognised market it may be difficult for investors to sell their investment or to obtain reliable information about their value or the extent of the risk to which they are exposed.

The information contained in this document is confidential and is solely for use of those persons to whom it is addressed and may not be reproduced, further distributed to any other person or published, in whole or in part, for any purpose.

CSL STOCKBROKERS LIMITED
Member of the Nigerian Stock Exchange
PO Box 9117
Lagos State, NIGERIA
W1s 2SA

CSL Stockbrokers
A trading name of CSL Capital (UK) Ltd
43-44 New Bond Street
London
United Kingdom