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FDC MONTHLY ECONOMIC UPDATE

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In This Issue ...

Nigeria Launches a New National Carrier –Hit or Miss?

Background

15 years after the liquidation of Nigeria Airways, the FGN formally initiated plans to float another national carrier at the end of Q4'18. The launch of the national carrier, which is expected to be private sector driven, is one of the current administration's major interventions in the aviation industry. This initiative is projected to boost Nigeria's African footprint, as well as create job opportunities in the sector.

The proposed airline is anticipated to ply 81 routes and will require as much as $300 million seed capital. To this effect, the Infrastructure Concession Regulatory Commission (ICRC) issued a conditional Certificate of Compliance along with the Outline Business Case (OBC). The 12-month certificate will enable the government commence a competitive bidding process for strategic investors to cater for seed capital, operation and management of the national car-

Lessons from Other National Carriers

Most national carriers have been performing sub optimally, both in revenue terms and average seat per kilometre. The industry has been plagued by losses, squeezed margins, high costs of fuel and security since the 9/11 terror attack. A number of key national carriers, such as British Airways, have had to be privatized to mitigate financial haemorrhage. Other national carriers, like Swissair (Switzerland's national carrier) filed for bankruptcy in 2002; Sabena (Belgium's national carrier), filed in 2001 after numerous years of unprofitability.

Particularly in Africa, uninformed interference has widely undermined the success of most national carriers, as very few of these airlines have been able to fully breakaway from government intervention and conflict of interest.

With the exception of Ethiopian Airlines, national carriers in Africa have been generally unprofitable. RwandaAir has declared annual losses since its inception in 2002; South African Airways has also experienced financial turbulence of recent, as the African Giant is in search of institutional investors to inject additional capital into the ailing airline; and Kenyan Airways has continued to reduce its fleet of aircrafts to narrow its operational losses.

Performance of African National Carriers in 2017			
Airline	**Revenue ($'Mn)**	**Profit/(Loss) ($'Mn)**	**No. of Aircraft**
South African Airways*	2,292	(415)	64
Kenyan Airways**	1,053	(101)	39
Ethiopian Airlines	2,710	233	92
RwandaAir***	100	(55)	10

[1]

Ethiopian Airline's success over the years hinged on aggressive expansion strategy. The airline operated a national carrier devoid of government interference and control despite being 100% owned by the Ethiopian government. In addition, the airline enjoys income streams from its maintenance, repair and overhaul (MRO), which serves numerous airlines in Africa.

Times have Changed

In view of the shifting competitive environment and the traction free trade is gaining, operating a national carrier has limited upsides. The popularity of trade policies such as the open skies agreement and the African Continental Free Trade Agreement (ACFTA) has led to the unattractiveness of operating a national carrier.

Hitherto, most trade agreements were bilateral. This resulted to the need for a flag carrier to facilitate the movement of people and goods between bilateral partners. However, since the emergence of multilateral trade and less protectionism, national carriers have had to compete internationally based on internal efficiencies and superior customer service delivery.

The history of FGN's participation in the aviation industry proves that Nigeria is at a competitive disadvantage. This is in light of its economic woes with Nigeria Airways, plagued by misappropriation and conflict of interests. Subsequent efforts to revive the national carrier through collaboration with Virgin Group also fell through due to political intrusion. This affirms that Nigeria is unequipped to successfully compete in the global market.

Is the Proposed National Carrier a Priority?

Air transport is a major facilitator of international trade being the preferred and fastest point-to-point transport medium across national borders. In Nigeria, the aviation sector contributes only 0.10%[2] to GDP, but the sector remains a key catalyst of economic growth and development. Despite the absence of a national carrier, 13.39 million passengers and 162 million kilogram of freight travelled to, from and within Nigeria in 2017. More than 39,000 international flights departed Nigeria, while another 175,000 flights operated domestically. Comparison with air activities before the cessation of Nigeria Airways established that the industry achieved significant strides without a national carrier. The most impressive is the 87% growth in passenger traffic from 7.16 million passengers in 2003.[3]

[1] Various Company Financials in 2016/17 ;*Mar'17; **9M'17; ***FY'16
[2] NBS GDP Report Q1'18
[3] NBS Air Traffic Data Q4'17

However, more pertinent issues stalling accelerated growth in the aviation industry is the wide infrastructure gap estimated at $30bn by aviation industry experts. Top on the list is the concessioning of the four major airports (Lagos, Abuja, Kano and Port Harcourt). This will ease the heavy burden on the government's budget and incorporate the much needed efficiency into airport management. The involvement of the private sector will boost investment, which will trickle down to other infrastructural deficits in the aviation value chain.

The absence of an MRO facility in Nigeria has cost local airlines over $500 million in capital flight. This has weighed in considerably on their costs, as well as the attractiveness of the industry. These constraints have left the industry unattractive to foreign and institutional investors. Consequently, investment in MRO facilities will ease FX denominated leakages and boost FX earning, especially from patronage of West African countries.

Moreover, the utilization of tax payers' funds to finance an unprofitable venture will show a high level of inefficiency. The opportunity cost of the $300 million seed capital for an airline for the elites is socially ineffective. The impact of a $300 million injection will have had greater social impact in key sectors, such as healthcare and power.

Recommendations

Focus on Infrastructure Injections

Remarkable breakthroughs can be recorded in cost and quality despite the limited economic resources at the disposal of the government. The priority of the government should centre on the concessioning of the busiest airports. This can be achieved with little or no cost to the government.

There is also the need to address technical issues in the air transport value chain to jumpstart growth in the aviation sector. These issues revolve around local aircraft MRO, as well as airport handling services and flight simulation centres. Tackling these infrastructural deficiencies will reduce airlines operation cost, as well as the attractiveness of the industry. Consequently, key industry stakeholders will move to complement government's intervention, creating a much more viable and sustainable framework for potential growth. Hence, the key to success is the full independence of airline operations from government's management and control.

Need for Extensive Stakeholder Engagement

Extensive stakeholder engagement is an essential framework that needs to be incorporated in the regulatory mechanism for decision making. This will mitigate error rates as a result of goal incongruence and increasing conflict of interest.

Essentially, private stakeholder engagement will facilitate the much needed capital injection, as well as the technical aptitude to efficiently deliver value in the aviation value chain. However, the onus is on the aviation public administrators to align the interest of institutional investors (RoI) and the FGN (social interest) in order to ride on the gains of globalization and international trade.

Is The Oil Price Rally Over?

Background

Since the month of March, oil prices have embarked on a three-month bullish streak, rising 19.5% to reach a 3½ year high of $79.44pb on June 29th. This was driven by four main events: i) the US- China Trade war, ii) US-Iran Sanctions, iii) declining US inventories, despite the 13.45% increase in rig count, and iv) dwindling global supply, as a result of lower output from Libya, Venezuela and Canada.

Since then, prices have lost 8.5% to $72.69pb as at July 20th. This turn-around of events was primarily caused by supply factors.

First, in accordance with its decision on June 29th in Vienna, OPEC and its allies have reduced compliance levels. Compliance rates fell to 120% in June, from a high of 147% in May and 181% in April. The oil bloc appears to be hearkening to President Trump's tweet for a call for lower prices.

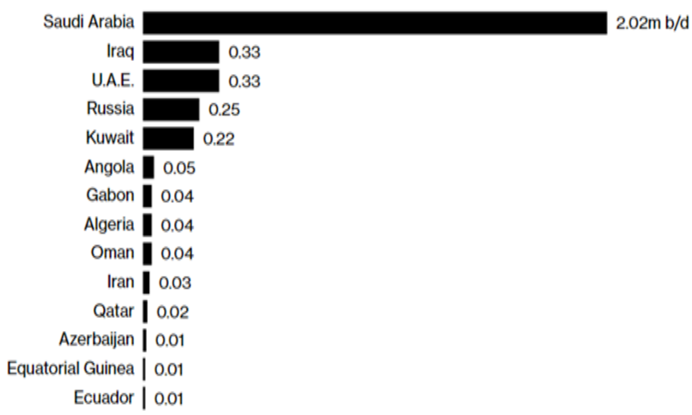
Secondly, in the week ending July 13th, the US output reached a record high of 11mbpd (the highest in history). Additionally, Saudi Arabia's output jumped 5.4% to 7.6mbpd – the highest monthly increase since 2016-end.

Factors that will affect short-term prices

Just like any other commodity, the price of oil is influenced by the market forces of demand and supply.

OPEC and its allies plan to reduce compliance to 100%. This is equivalent to an addition of 1mbpd to the market, compared to April. However, in reality this figure could be as low as 700,000mbpd, due to the lack of spare capacity. Spare capacity refers to the ability of oil producers to ramp up production in response to global supply disruptions. At the moment, most oil rich countries, with the exception of Saudi Arabia, are already producing close to maximum capacity.

Chart showing the excess capacity of major producers



Source: International Energy Agency

Nevertheless, OPEC production is expected to continue to inch up in the coming months. Likewise, Canada's Syncrude is expected to resume operations by first week in August (latest). For Libya, it is less straightforward. After the resumption of the National Oil Corporation's (NOC) exports, and the re-opening of El Feel oil field in early July, another major oil field has declared force majeure following the kidnapping of two staff. Political and military division would continue to pose threats to Libya's output in coming months.

US President Trump has issued a deadline of November 4th, to its allies to completely stop the importation of Iranian oil. Iran's biggest importers include China, India, South Korea and Turkey. If these countries comply, this could potentially mop up approximately 1mbpd from the global market. Nevertheless, comments from China and India have suggested that they may not be quick to take the US' side. Meanwhile, Iran has taken the US to the International Court of Justice on the grounds that Iran has abided to the rule of law, and thus such sanctions against it are unlawful.[4] The jury is out as to what the allies will do in the coming months. Until then, the suspense around the sanctions would keep market expectations bullish. This will partially balance out the effect of higher global supply from OPEC and its allies, the US and Canada.

Given these considerations, we expect the price of oil to dip further by 1%-3% to an average of $70pb-$72pb in the short term (4-8 weeks).

Implications

At $70pb, oil prices would be 5.3% higher than the price at the beginning of the year, and 40.85% higher than prices a year ago.

Also, this price level is 30.77% higher than the budget benchmark of $52pb, and is still sufficient to support fiscal spending, with enough leeway for national savings. Thus, Nigeria's trade balance would remain in surplus territory, as export earnings remain relatively robust. These earnings would also be able to support the external reserves, the naira and the ongoing recovery process.

[4] OilPrice.com <https://oilprice.com/Geopolitics/Middle-East/Iran-Files-Complaint-Against-US-For-Unlawful-Sanctions.html>

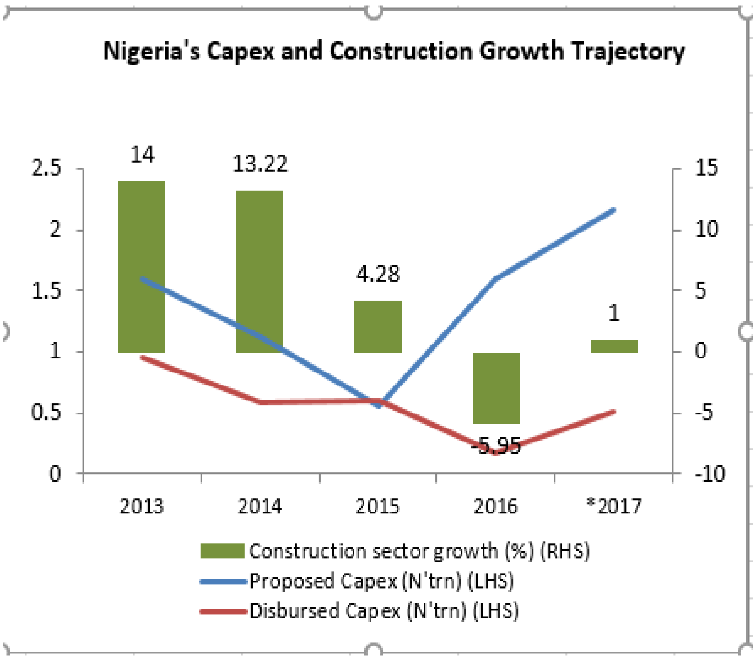
The month of June witnessed some noteworthy events of significant implications for the construction sector. In Nigeria, these range from the presidential assent to the 2018 budget, the federal government's announcement of a new building code and Julius Berger's introduction of a technology that would guarantee roads durability of in the country. On the SSA front, construction activities have shown progress ahead of the 2019 African Cup of Nation (AFCON) scheduled to be held in Cameroon.

Nigeria's Construction Sector in June

The 2018 Budget and the construction Sector

President Buhari signed the 2018 appropriation bill into law on June 20 after a 7-month delay by the National Assembly. The N9.12trn budget earmarks N2.87trn (31.5%) for capital vote, 32.26% above the 2017 proposed capex.

The sharp increase in capex allocation should have been good news for the construction sector. However, historical evidence suggests that Nigeria typically under spends its proposed capital expenditure. Meanwhile, construction sector performance has been more correlated with the actual disbursements for capital vote than the amount proposed in the appropriation bill.



[5]

Nigeria's capex and construction growth trajectory

Between 2013 and 2015, Nigeria's actual capital spending was below the proposed amount with the exception of 2015. The construction sector's performance moved in tandem with these actual disbursements. For instance, in 2016, when actual capex declined sharply by 71.7% to N170bn, the construction sector recorded a negative growth of -5.95%. In 2017, when spending increased to N510bn, the construction sector's growth picked up to 1%. It is expected that the country would under spend the 2018 proposed capex budget as empirical evidence suggests. Moody's Investors Services shares the same view, stating that the capital expenditure portion of the 2018 fiscal plan is unattainable. However, we expect that relatively high oil prices would support revenues and enable the government disburse more funds for capex in 2018. This should translate to a quicker growth for the sector in the year.

[5]Nigerian Bureau of Statistics, Budget Office, FDC Think Tank

Federal Government announces new national building code

The Federal Government, through the Minister for Power, Works and Housing, Mr. Babatunde Fashola, announced a new national building code. The new code will regulate construction activities with the aim of improving on measures to safeguard lives and properties in the country. The government has come up with the new code on awareness of the fact that most deaths and injuries caused during building collapse are results of unacceptable ways of building. According to the minister, houses will now be designed in such a way that public safety cannot be compromised.

Implications

Between 2012 and 2016, total number of collapsed buildings in the country stood at 54.[6] The number of deaths associated with these collapses in unascertainable. These collapses and deaths have been largely due to wrong plans and structures. The new code by the Ministry of Power, Works and Housing is expected to reduce the risks and number of deaths associated with wrong plans for buildings and other construction projects in the country.

Julius Berger Nigeria introduces new technology to road construction

According to the Managing Director of Julius Berger Nigeria (JBN), JBN has introduced a new technology to the construction of roads in Nigeria. The new technology involves the grounding of the old asphalt, treating it and using it to increase the thickness and height of the asphalt for lasting roads. The company, with the new technology, would construct more lasting roads with an asphaltic concrete thickness of 12 centimetres (120mm).

Implications

An improvement in road thickness is expected to make Nigerian roads more durable. Road transport constitutes the major means of moving goods and people within the country. The advancement of the sturdiness of these roads would also reduce government expenditure on road repairs and maintenance. This should allow the government channel its finances towards the expansion of the existing road networks to ease movement. A wider road network would have a greater positive impact on economic activities and inclusive growth.

FG pledges support to indigenous contractors

The Minister of Science and Technology Dr. Ogbonnaya Onu, urged indigenous contractors under the umbrella of the Association of Indigenous Construction Contractors of Nigeria to bolster their skills and competiveness to enable them bid and compete for jobs in other parts of the world. The minister pledged support for all Nigerian professionals in the award of contracts in the infrastructural development sector.

Implications

The intent signalled towards the prioritization of the service of indigenous contractors is positive for the reduction of

[6]Federal Ministry of Power, Works & Housing, 2017. "Communiqué of The 6th Meeting of The National Council on Lands, Housing And Urban Development". Federal Government of Nigeria, http://www.pwh.gov.ng/download/15036674409697.pdf

SSA

Construction activities progress ahead of AFCON games

The Governor of the Littoral region, Mr. Samuel Dieudonné Ivaha Diboua, inspected the project sites in Douala, Cameroon ahead of visits by the Prime Minister and the Confederation of African Football (CAF) inspection team. After the visit, the Governor expressed satisfaction over the progress of work. He however recommended the acceleration of work by recruiting more manpower and acquiring more equipment. Work at the Japoma stadium which would host some group matches, is completed by 51% generally. At the Mbappe Leppe and Bonamoussadi stadiums which are supposed to serve as training grounds, work has been completed by 38%. At the Reunification stadium, 15% of work is completed.

Implications

Significant technical progress would be necessary for Cameroon to maintain its grip as the host nation for the 2019 AFCON games. The hosting of the game is expected to boost forex inflows into Cameroon. Ancillary commercial services such as transport, hospitality and financial services are poised to benefit from this.

Construction Companies' Performance on the NSE in May

Three out of the 169 listed companies on the Nigerian Stock Exchange (Julius Berger Plc, Arbico Plc and Roads Nigeria Pl) are construction firms and they constitute approximately 0.3% of total market capitalization. The stock prices of these firms lost an average of 0.06% in June. Share prices of Arbico and Road Nigeria were flat in the month. Julius Berger lost 0.18% in the last month.

Company	Share Price (May) (N)	Share Price (June) (N)	%Change	Directional Movement
Julius Berger Plc	27.55	27.50	-0.18	⬇
Arbico Plc	4.79	4.79	0	⟷
Roads Nigeria Plc	6.60	6.60	0	⟷

Outlook

We expect rains in July to widely constrain construction activities. We however expect some intent towards the construction of new projects after the part-disbursement of the 2018 capex budget. We are also likely to see some preliminary activities towards the completion of abandoned projects as the political environment gets heated ahead of the 2019 polls.

Power Sector Reforms

The Vision 20:2020 economic plan was launched in 2009 to drive Nigeria towards becoming one of the top 20 economies in the world by the year 2020. This plan had several goals including the generation, transmission and distribution of 35,000MW of electricity by the year 2020. Although power generation capacity has increased significantly from a paltry 3,500MW in 2008 to 7,500MW as at May 2018, it is insufficient for a country the size of Nigeria. Normally, electricity generation capacity should correlate with the population of a country. For instance in 2016, South Africa generated 40,000MW for 50 million people, Brazil generated 100,000MW for 207 million people and the United States generated 700,000MW for 320 million people.

Eleven years have passed since the Vision 2020 plan was birthed and there is already a massive shortfall between the planned and actual. The plan was to achieve 16,000MW by 2013 but Nigeria is still struggling to generate on-grid power output of 4,500MW mid-way through 2018. The dependence on thermal generation and inability of the government to ensure gas supply has kept the country behind some of its peers. For instance, gas constraints have averaged 1,800MW in the last three months, 47% of total output. The tepid progress in increasing power generation in Nigeria is not new. Preceding Vision 2020 was the Electric Power Sector Reform Act of 2005 (EPSR), which was the foundation for power sector improvements. However, no major improvements. This is very disconcerting considering that the contents of Nigeria's reforms are similar to those in some other countries. So why has there not been a surge in Nigeria's power generation?

Case Study of Vietnam

Vietnam has a population of about 90 million representing almost half of Nigeria's population. Similarly, Vietnam's GDP of $123.6bn is paltry when compared to Nigeria's $405.1bn. As a member of the Next Eleven Economies (countries with high potential to become the world's largest economies in the 21st century along with the BRICS) which also includes Nigeria, Vietnam recognized the need for power improvements to support its growth over the years. As a result, the country embarked on power reforms which started in 2005 when a new electricity law came into effect.

Through the establishment of the new electricity laws, Vietnam aimed to:

- Expand and improve the power system (resource development) through the development of competition
- Enhance the transmission lines
- Reduce transmission and distribution losses

The Vietnamese government created competition in the power sector which drove the expansion and improvement by:

- Investment by the state-owned Vietnamese Electricity
    - Generation and distribution companies became different units under a holding company (similar to the Power Holding Company of Nigeria)
- Build-Operate-Transfer (BOT) by granting concessions for construction and development
- Independent Power Projects (IPP) through the participation of private capital

Vietnam's installed generation capacity was able to grow from 11,578MW in 2005 to 24,500MW in 2016 with transmission and distribution losses reducing by an annual average of 0.6% in the same period. However, the generation capacity in Nigeria, which can be grouped with these countries, has basically remained flat throughout this same period.

Lessons for Nigeria

There is a lesson for Nigeria to learn from Vietnam's power sector progress. Just like Vietnam, Nigeria's power sector reforms involved changing the structure of the sector to separate generation, distribution and transmission units. Vietnam was able to effectively create competition in the sector while Nigeria has not succeeded in achieving this so far. The defining and key factors which made the difference in the two countries over the past years are reduced corruption in the sector better management.

The government of Vietnam was able to show better management of the power sector which attracted the needed investments into the sector. Even though Vietnam has a notorious reputation for endemic graft, the government was able to stem this corruption to allow progress in the power sector.

Corruption and poor management have been highlighted as the cause of the poor state of Nigeria's power over the years. The privatization of the generation and distribution companies in 2013 has been stalled due to these same factors. Effectively removing these factors from the sector will hasten the reforms and attract the needed investments that would create competition, diversify the generation mix from thermal and hydro generation and aid in the development of the human capital needed to support the reforms.

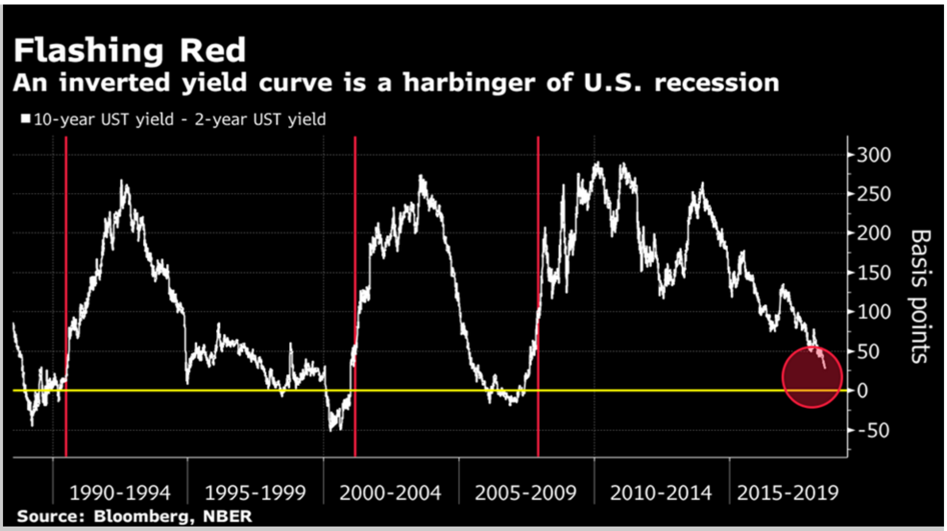
Notable developments in the power sector

Multilateral organizations raise $1.57bn to expand Nigeria's power grid

Multilateral organizations such as the World Bank and African Development Bank (AfDB) have raised $1.57bn for the Transmission Company of Nigeria (TCN) to expand Nigeria's electricity grid to 20,000MW by 2023. The funds were raised to implement the TCN's Transmission Rehabilitation and Expansion Programme (TREP). An increase in power output would support growth in the manufacturing sector and boost aggregate output.

Run-Up to U.S. Recession Is Good Time for Emerging Markets

Global Perspective: *Culled from Bloomberg*



"If the end of easy money, a trade war and myriad geopolitical dangers weren't enough, a U.S. yield curve poised to invert is adding to the risks for investors. But there's one asset class that's less of a worry: emerging markets.

Every time the yield curve has flipped in the past three decades, sending shorter-term interest rates above longer-term ones, the U.S. economy has entered a recession within 12 to 24 months. While that correlation makes the inverted curve a risk-off signal, it's been a different story with emerging-market assets.

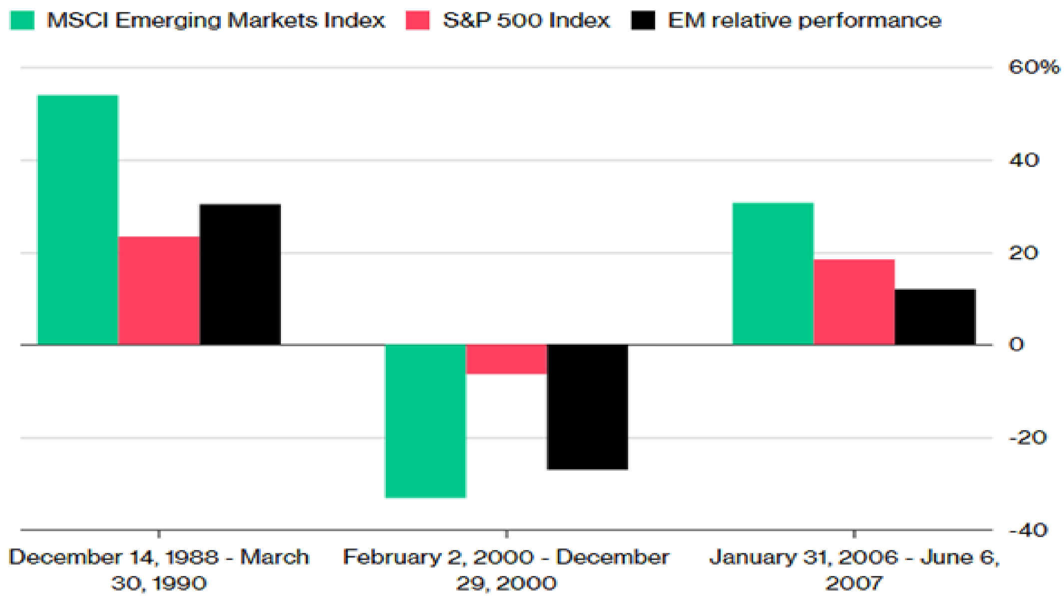
History suggests that the inversion has no influence on emerging markets. At best, it might be a bullish signal. Developing-nation stocks outperformed U.S. equities when the spread between 10-year yields and 2-year yields was negative in the run-up to a recession in 1990 and 2007. They trailed U.S. stocks in 2000, before the economy started contracting the following year, leaving the score at 2-1 in favor of emerging markets.

With bonds and currencies the picture is more clear-cut. Both climbed against U.S. assets in the last two recessions (data before the 1990 recession isn't available). Investors also cut the risk premium for owning emerging-market sovereign dollar bonds rather than U.S. Treasuries on both occasions.

Developing-nation assets react to many external and idiosyncratic factors, and the yield curve isn't able to influence their moves compared with those factors, according to William Jackson, an economist at Capital Economics Ltd. in London. But once a U.S. recession gets entrenched, it might affect risk appetite, pushing emerging markets toward underperformance, he said.

Risk-On Regardless

On two of past three times yield curve inverted, EM stocks outperformed U.S.



Source: Bloomberg
Note: Returns from date of yield-curve inversion to date of normalization

The spread between 10-year and 2-year yields is at 27 basis points, the lowest since August 2007. Similar gap between 7-year and 2-year rates is at 24 bps, the narrowest since at least 2009. The 5-year rate is just 17 bps away from the 2-year one. They all continue to fall as growing concern about a recession is pushing investors to buy longer-dated Treasuries, while Federal Reserve rate increases are boosting the yield on shorter-term bonds.

July marks the 109th month of continuous economic expansion in the U.S. after it emerged from the last recession in June 2009, according to the National Bureau of Economic Research. That's the second-longest phase of growth since 1854, beaten only by a 120-month stretch in the 1990s. The law of averages dictates that it's a late-stage economy and a recession may be closer than the markets are pricing in.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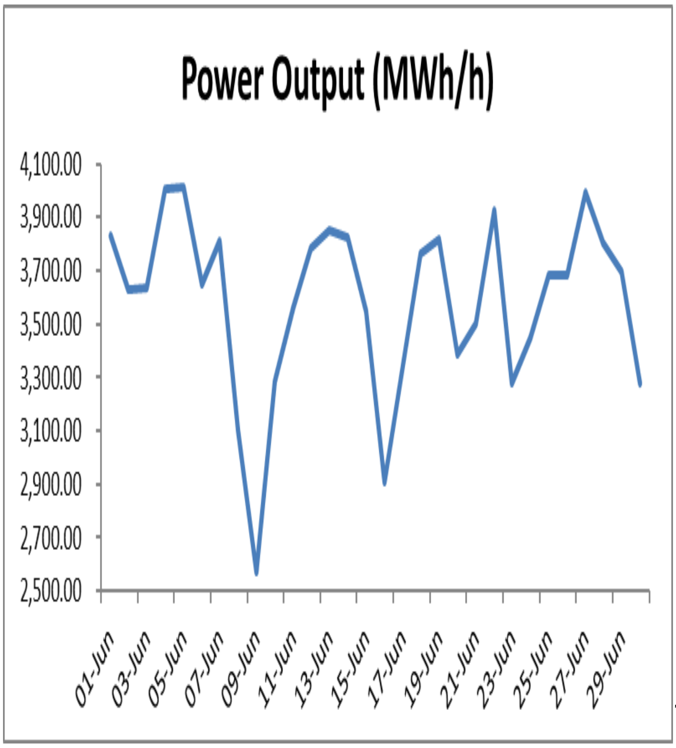
Macroeconomic Indicators

Power Sector

The average on-grid power output in June was 3,588MWh/h, a 5.08% decline compared to the average of 3,780MWh/h in May. This decline was as a result of insufficient gas supplies amid distribution and frequency constraints. Gas shortages remained the dominant constraint in the month, representing about 65% of the total constraints (89,641MWh/h). During the month, average power output touched its lowest year-to-date level of 2,572MWh/h on June 9th, following the grid collapse on June 8th. The confluence of the gas pipeline rupture on June 15th and technical issues at the Shell gas wells on June 16th led to the shutdown of six power generating plants. The sector lost approximately N43.03bn, annualized at N7.23trn.



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Outlook

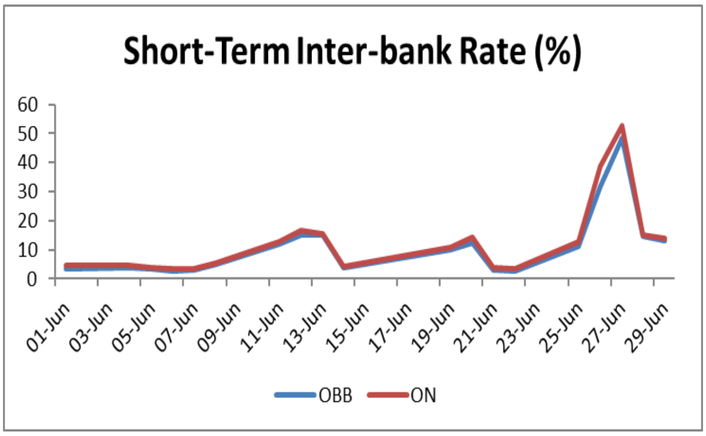
We anticipate an improvement in hydro-generated power as rainfall intensifies in July. This is expected to impact positively on power output, barring any rupture in gas pipeline. In a bid to support Nigeria's economic growth plans, the World Bank has approved a total of $2.1bn concessionary loan to fund projects in the country. Half of the loan is expected to be used in financing power and climate change projects. The successful implementation of this project is expected to have a long term benefit on power generation.

Money Market

The average opening position of the interbank money market increased sharply by 85.30% to N312.05bn long in June from N168.40bn long in the preceding month. This increase in the opening position reflects increased liquidity, which filtered through to a sharp drop in the average short-term interbank rates. The average short-term interbank interest rates (OBB, O/N) recorded a sharp decline of 831bps to 11.94% p.a. from May's average of 20.25% p.a. The open buy back (OBB) and Overnight (ON) rates climbed to a high of 48.33% p.a and 52.58% p.a respectively on June 27, due to the CBN's wholesale forex debit before declining to close the month at 13.17% p.a and 14.08% p.a respectively.

The CBN issued more OMO bills in June. However, there were less OMO maturities. This resulted in total net outflows of N60bn compared to the net inflows of N310bn recorded in May.

[7]FGN, FDC Think Tank



[8]

At the primary market, the yields on the 91-day and 182-day T/bills declined while that of 364-day T/bills was flat. Conversely, yields in the secondary market increased for the 91 -day and 182-day tenor but declined for the 364 day tenor.

Primary Market

T/bills Tenor	Rate on June 13th (% pa)	Rate on June 20th (%)pa	Direction
91	10.2	10.0	↓
182	10.5	10.3	↓
364	11.5	11.5	↔

Secondary Market

T/bills Tenor	Rate on June 1st (% pa)	Rate on June 29th (%)pa	Direction
91	11.79	12.40	↑
182	11.67	12.27	↑
364	12.62	12.57	↓

Outlook

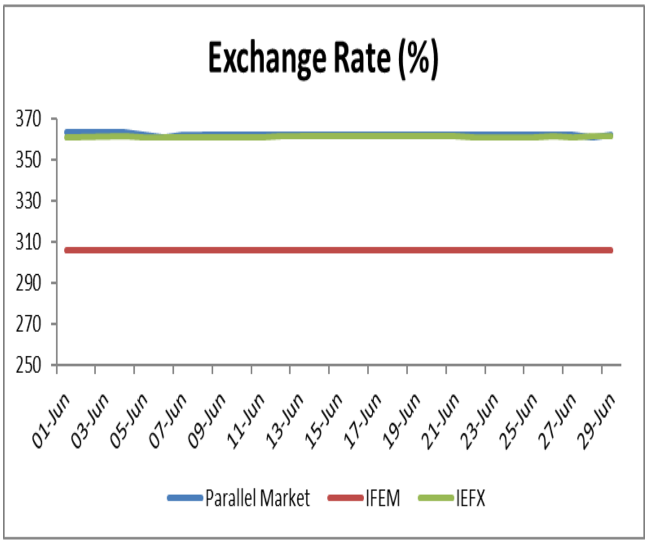
We anticipate a boost in market liquidity owing to the disbursement of budget funds. This is likely to keep interest rates at low levels. However, we expect the CBN to continue with its usual intervention scheme to mop up excess liquidity. The MPC would be meeting on July 23rd and 24th to deliberate on the fate of the monetary policy parameters. Some of the major considerations are the sustained moderation in inflation rate, weak and tepid GDP growth. The risk of a reversal in the trajectory of the inflation rate will also be considered.

Forex Market

Exchange Rate

At the parallel market, the naira opened at N363/$, appreciated to N361/$ (a 2-year high) on June 6th before depreciating to close the month at N362/$. The naira appreciated at the interbank foreign exchange market to close at N305.75/$ from N306/$ on June 1st. At the IEFX window, the naira traded within the tight band of N360.95/$-N361.32. The total turnover at the IEFX window was $4.38bn, 17.20% lower than $5.29bn in May. The CBN sold forex worth $2.20bn in the month.

[8] FDC Think Tank



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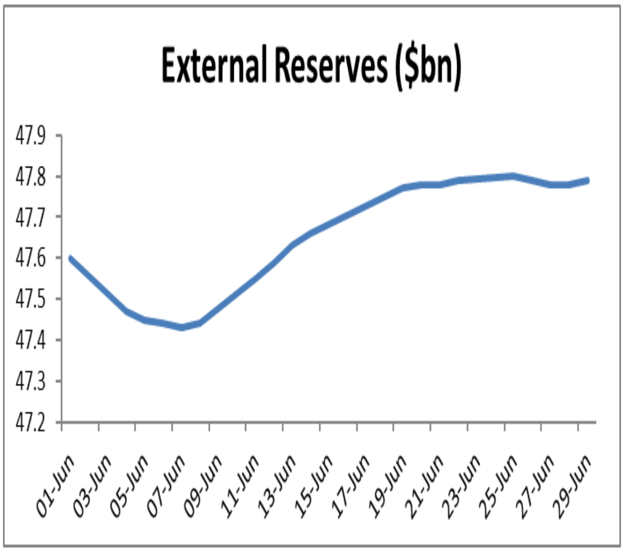
Outlook

We anticipate an increased demand for forex, following the disbursement of funds for capital project. This coupled with the speculative demand from tourists could mount pressure on the naira. Hence, the naira is projected to depreciate marginally to N363/$-N365/$ in the near term.

External Reserves

External reserves recovered after recording a steady decline in the first few days of the month. The external reserves increased by 0.74% to close at $47.79bn on June 29 from $47.44bn on June 8. The country's gross external reserves increased despite the CBN's intervention of $2.20bn during the month, which is higher than May's value of $1.43bn. The accretion in external reserves has increased the import cover from 11.66 months to 11.7 months.



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Outlook

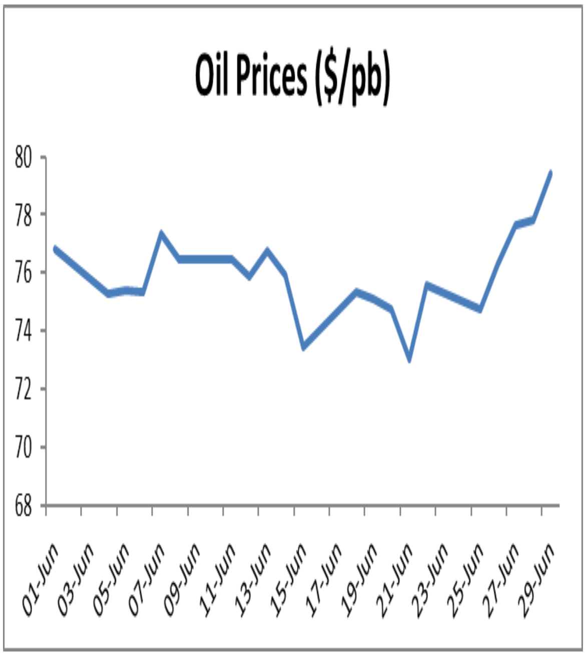
The disbursement of funds for CAPEX could trigger an increased demand for forex. To ease this pressure, the CBN could continue with its usual interventionist mechanism. This could be at the expense of depleting the reserves.

[9] CBN, FMDQOTC, FDC Think Tank
[10] CBN, FDC Think Tank

Commodities market - Exports

Oil prices

The average price of Brent crude declined marginally to \$75.94pb in June from the average of \$77.01pb in May. During the month, oil futures touched a low of \$73.44pb on June 15th, its lowest level since May 2nd. This decline was largely driven by concerns about rising OPEC and Russian supplies. Despite the decline, oil prices remained comfortably above \$75pb, which is higher than Nigeria's 2018 budget benchmark of \$51pb. This is positive for government foreign earnings, reserves and excess crude account.



[11]

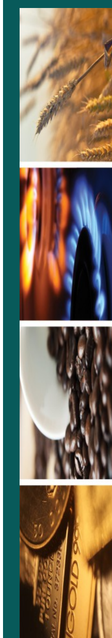
The Organization of Petroleum Exporting Countries (OPEC) held its first bi-annual meeting for the year in Vienna on June 22nd in order to review the progress in the oil market. At the meeting, it was agreed that production should be raised by one million barrels per day. However, a major concern of this development remains the supply disruption in some OPEC member countries such as Venezuela, Libya, Iran and Angola. Owing to this constraint, it is likely that the effective increase in supply could be lower than the set target.

Outlook

Oil prices are expected to remain above \$75pb in the near term, owing to the fact that the markets have already factored in the expectations of a quota increase. Growing demand during the summer period could further support crude prices. However, the downward risk to this is the possibility of political pressure on OPEC from the US to push down prices in coming months.

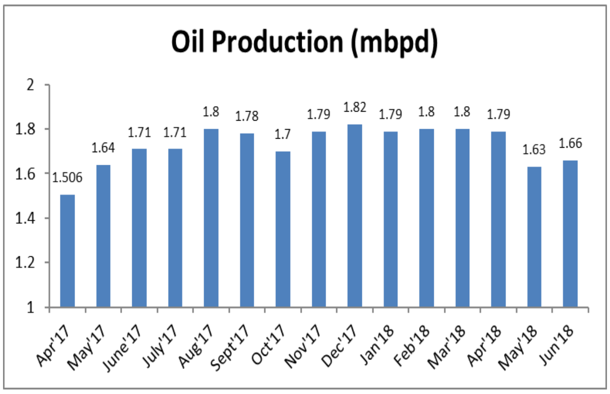
Oil Production

Nigeria's oil production increased marginally by 1.84% to 1.66mbpd in June from 1.63mbpd in May. Despite the increase, oil production still falls below the 2018 budget benchmark of 2.3mbpd. During the month, the Trans-Forcados and Nembe Creek pipelines were shutdown due to leakages and ruptures. As a result, the operators declared force majeure for the export of Bonny Light. Nigeria's oil rig count declined to 13 in June from 14 in May.[12] This signifies the possibility of a decline in production in the coming period, which may reduce Nigeria's prospect of benefitting from OPEC's decision to increase global output. In Q2'18, oil production averaged 1.69mbpd, which is 5.06% lower than the average of 1.78mbpd in Q1'18. This was partly due to the supply disruptions recorded in the quarter.



[11] Bloomberg, FDC Think Tank

[12] Bakers Hughes



[13]

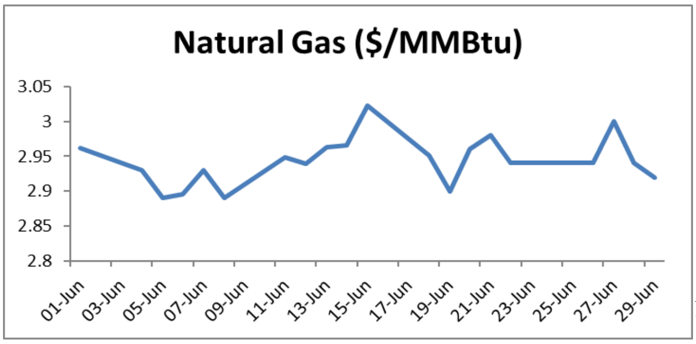
Outlook

The closure of the Trans-Forcados and the Nembe Creek pipelines could result to a decline in oil production in the coming month. However the anticipated decline in production is trivial compared to the gains made in prices. Nigeria's oil revenues should remain relatively unchanged.

Natural Gas

Natural gas prices dipped 1.42% to $2.92/mmbtu on June 29th from $2.96/mmbtu on June 1st. During the month, natural gas price rose to a 4-month high of $3.02/mmbtu. The average price in the month was $2.94/mmbtu compared to May's average of $2.83/mmbtu. The increase in price was mainly due to the oil price rally and increased demand for gas.

As part of an effort to bridge gas supply shortfalls in the country, the Nigerian National Petroleum Company (NNPC) has signed an agreement with Shell, Seplat and Oando to implement seven gas development projects which is worth $3.7billion.



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Outlook

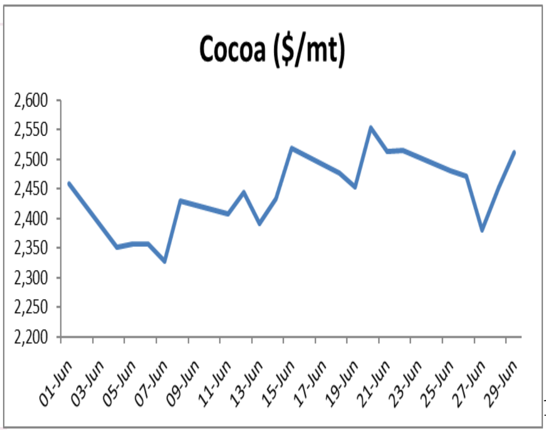
The natural gas project is expected to have a long term impact on Natural gas supply. Increased supply of natural gas will help to keep prices low.

Cocoa

Cocoa prices increased by 2.20% to close the month at $2,512/mt from $2,458/mt on June 1st. The average price of cocoa was $2,442/mt in June, 9.32% lower than $2,693/mt in May. This decline was triggered by investors' expectations of an imminent increase in production from top growing countries, Cote d'Ivoire and Ghana, coupled with lower demand from top importers in the UK. Cote d'Ivoire, the world's largest producer of cocoa is projecting a production of about 9 million tonnes, while Ghana is planning to increase output by one million metric tonnes. The favorable weather conditions in key growing regions also supported production, driving down prices.

Outlook

Ghana's plan to increase output by one million metric tonnes without a corresponding increase in demand could compound the decline in cocoa prices in the coming period. The sustained decline in cocoa prices would weigh on farmers' revenue and profitability. This could lead to a reduction in farmers' investment in the sector.



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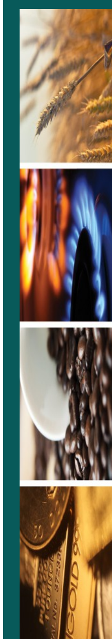


[13] OPEC, FDC Think Tank

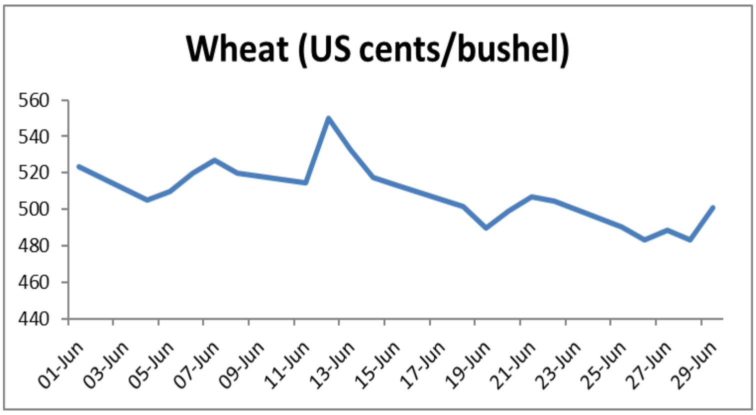
[14] Bloomberg, FDC Think Tank

[15] Bloomberg, FDC Think Tank

Commodities market - Imports

Wheat

Wheat prices declined 4.20% to $5.01/bushel on June 29th from $5.23/bushel on June 1st. The average price of wheat in June was $5.09/ bushel, 1.60% lower than May's average of $5.17/bushel. The decline recorded during the month was due to the improvement in US weather conditions.



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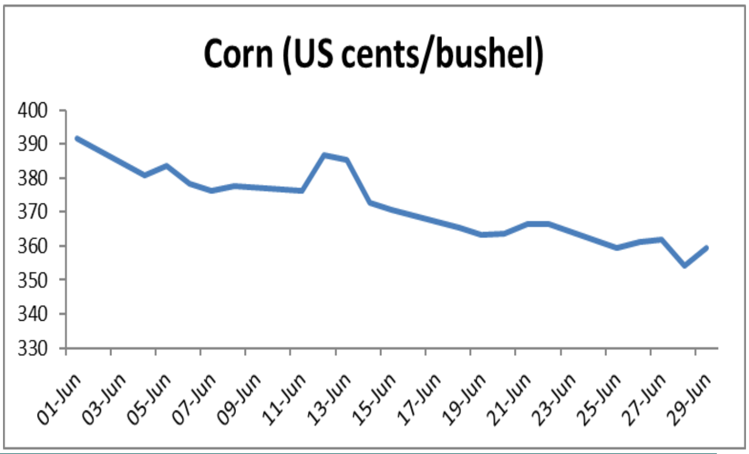
Corn

Corn prices slumped 8.17% to $3.60/bushel from $3.92/bushel on June 1st, supported by favorable weather condition amid improvement in the quality of corn crop in the US. The average price of corn was $3.72/bushel in June, 7.54% decline compared to the average of $4.02/bushel in May.



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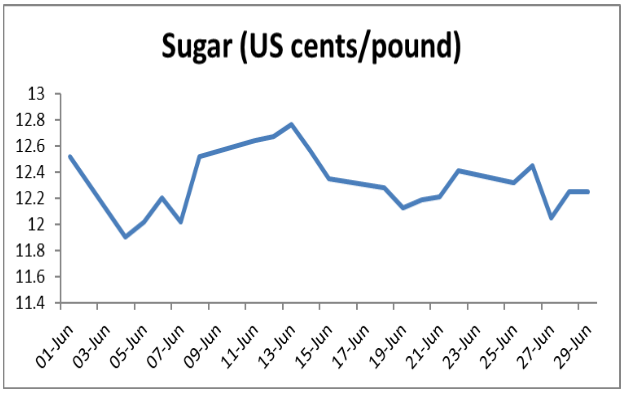
Outlook - Grains

We expect grain prices to trend downwards in July, driven by optimum weather conditions in major planting countries such as the US.

Sugar

The average price of sugar advanced 4.14% to $0.1232/pound in June from the average of $0.1183/pound in the preceding month. Sugar prices declined by 2.16% to $0.1225/pound on June 29th from $0.1252/pound on June 1st, resulting from ample global supply.



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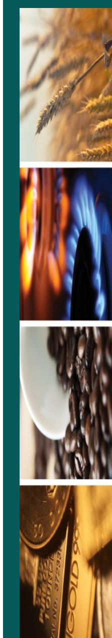
Outlook

The growing concern on the health implications of sugar has limited global demand. However, supply has been increasing in key regions (such as India). This is expected to keep sugar prices at lower levels in the coming period.



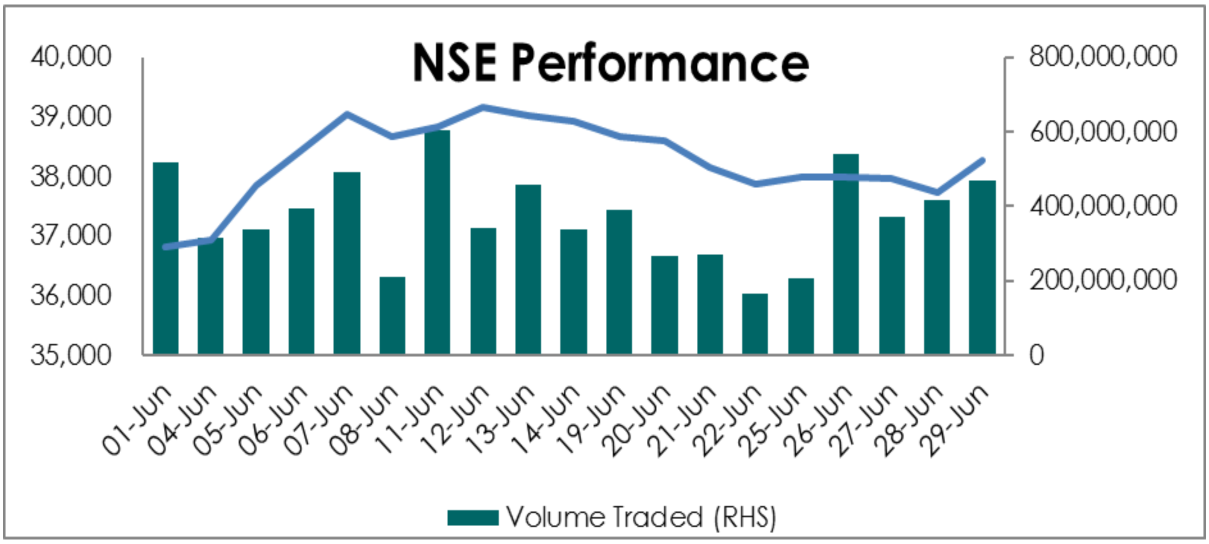
[16] Bloomberg, FDC Think Tank
[17] Bloomberg, FDC Think Tank
[18] Bloomberg, FDC Think Tank

Stock Market

Bear market dispels the correlation between oil prices and equities, as 2018 bucks the 5-year trend. So far in 2018 (H1'18), NSE ASI struggled to remain in the green, recording a negligible gain of 0.09%. However, during the same period, Brent prices rallied 18.8% to close H1'18 at $79.44pb.

The Nigerian stock market turned the corner in June 2018, after four consecutive months of losses. NSE ASI recorded a marginal gain of 0.46% to close at 38,279 points. Market capitalization moved in tandem with ASI, rose by 0.51% to N13.87trn in June. The tepid appreciation can be attributed to investors taking position in stocks with robust interim dividend history in anticipation of H1'18 interim dividend.

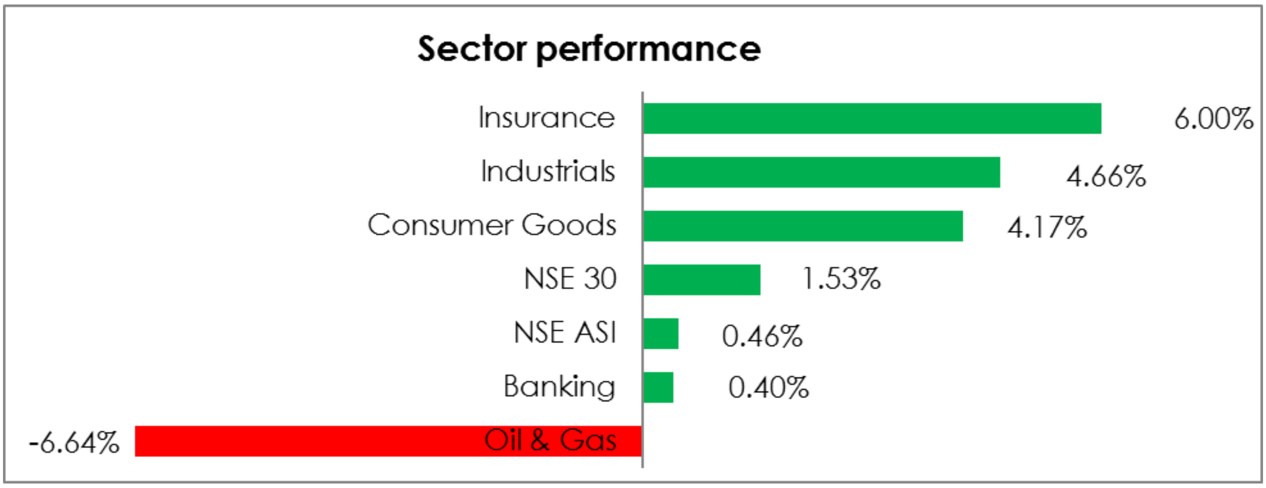
The bourse is currently trading at a price to earnings (P/E) ratio of 10.79x. This is a marginal decline over the close of the previous period's P/E of 10.89x. However, market breadth came in higher, but remained negative at 0.84x, as 41 stocks increased, 79 stocks remained flat, while 49 declined; compared to May, which came in at 0.47x.



[19]

Trading activities on the floor of the NSE established that the stock market remained liquid in the month of June. Average volume traded increased by 5.06% to 374 million units, but value traded moved in the opposite direction, declining by 35% to N4.94bn. This emphasizes investors' interest in undervalued penny stocks.

Stocks in the financial services sub sector dominated market transactions during the period. Financial institutions stock activities accounted for 76% of volume traded on the bourse in June.



[20]

[19] NSE, FDC Think Tank

[20] NSE, FDC Think Tank

SECTOR PERFORMANCE

All indices closed the month of June in green with the exception of the oil and gas sub sector index. The index lost 6.64% in June despite the oil price rally. The sector was dragged down by heavyweights in the sector. Positive investor sentiments waned, as investors were largely unimpressed with the performance of the large oil and gas firms.

Insurance sub sector index was the best performing index in June, as it increased by 6%. Most stocks in the insurance sector have been largely undervalued. This provided arbitrage opportunities for both speculative and long-term investors. In addition, insurance companies with lower combined ratio, which assesses internal efficiencies, boasted of considerable upsides.

Penny stocks dominated the gainers' chart, largely attributed to bargain hunting on undervalued stocks. Japaul Oil (71.4%) led the advancers, followed by C&I Leasing (55.6%), NEM Insurance (25%), Ikeja Hotel (24.7%) and Fidelity Bank (21.1%).

Top Gainers

Symbol	Jun 29 '18 Price	May 31 '18 Price	Change	% Change	PE Ratio
JAPAUL OIL & MARITIME SERVICES PLC	0.36	0.21	0.15	71.4%	-
C & I LEASING PLC.	2	1.33	0.74	55.6%	3.24
N.E.M INSURANCE CO (NIG) PLC.	3.20	2.56	0.64	25.0%	4.48
IKEJA HOTEL PLC	3.13	2.51	0.62	24.7%	10.54
FIDELITY BANK PLC	2.30	1.90	0.40	21.1%	3.48

Pharmaceutical and oil & gas stocks led the laggards with Neimeth (-13.6%) topping the chart. Seplat (-12.5%), Consolidated Hallmark (-12.1%), May & Baker (-11.7%) and Forte Oil (-11.2%) also featured among the decliners.

Top Losers

Symbol	Jun 29 '18 Price	May 31 '18 Price	Change	% Change	PE Ratio
NEIMETH INTERNATIONAL PHARMACEUTICALS P	0.57	0.66	- 0.09	-13.6%	-
SEPLAT PLC	650	743.20	- 93.20	-12.5%	4.69
CONSOLIDATED HALLMARK INSURANCE PLC	0.29	0.33	- 0.04	-12.1%	5.58
MAY & BAKER NIGERIA PLC.	2.34	2.65	- 0.31	-11.7%	17.24
FORTE OIL PLC.	32.85	37.00	- 4.15	-11.2%	3.24

Corporate Disclosures

Flour Mills Nigeria (FMN) Plc

FMN Plc posted a 3.5% increase in top line revenue to N542bn in its full year report ended March 2018. Profit before Tax (PBT) surged by 58% to N16.5bn, while Profit after Tax (PAT) moved in the same direction, rose by 54% to N13.6bn. Furthermore, Earnings per share (EPS) rose by 59% to N4.83/share during the same period.

Honeywell Flour Mills Plc

The company's revenue rose by 34% to N71.5bn for the full year ended March 2018. PBT declined by 11% to N4.9bn, but PAT moved in the opposite direction to record a growth of 3% to N4.4bn. EPS also recorded a marginal growth of 3% to N0.56 during the period.

Cement Company of Northern Nigeria (CCNN) Plc

CCNN Plc recorded a sharp increase of 204% in revenue in its full year financial statement ended March 2018, as revenue came in higher at N2.9bn from 0.9bn in the previous year. However, CCNN's loss before tax worsened from –N8.8bn to –N113.2bn in 2018. As a result, loss for the year increased by 238% to –61bn with EPS remaining negative at –N0.38.

OUTLOOK

H1'18 financial results will drive performance on the bourse in the short-term. In addition, growing uncertainties and speculations will exert pressure on the performance of the NSE. However, investors will continue to take position in stocks with robust interim dividend payment history, especially the banking stocks.


NASCON
Every meal starts with us
DANGOTE
Salt
Refined & Iodized
DANGOTE
Tomato Paste
Dan-Q
SEASONING
• Salt (Refined and Iodized) • Seasoning (Cubes and Tablets) • Tomato Paste • Vegetable Oil
www.nasconplc.com
Available nationwide.

Equity Report :

Conoil PLC

Analyst Recommendation: HOLD

Market Capitalization: N18.7bn

Recommendation Period: 365 days

Current Price: N28.00

Industry: Petroleum and Petroleum Products

Target Price: N25.50

Analyst's note

Circa 36% revenue growth

Conoil posted revenue of N115.53bn in FY'17, a 35.86% increase compared to N85.02bn in the preceding year. All its revenue was made from the sale of its petroleum products. Its white products segment contributed approximately 96% (N110.43bn) to revenue. The significant 38.28% growth in the sale of its white products offset the 1.61% decline in the sale of lubricants (N5.08bn in FY'17 from N5.16bn in FY'16).

Although Conoil's revenue increased, it had the least revenue among major oil marketers. Total Nigeria was the market leader with revenue of N288bn. Forte Oil came in second place with revenue of N129bn in FY'17.

Rise in finance costs pressure earnings

Conoil struggled to manage its costs effectively in 2017. It recorded a 44.56% increase in its cost of sales to N102.46bn from N70.88bn in FY'16. This was driven by a 46.04% and 9.65% increase in the cost of sales of white products and lubricant segments respectively. White products accounted for 97% (N99.28bn) of cost of sales.

The company posted a 21.09% increase in its finance cost to N2.14bn in FY'17 from N1.76bn in the previous year. This was primarily due to delays in the payment of subsidy claims by the Federal Government of Nigeria (FGN) on the importation of products for resale. In addition, it recorded a 40% (N11.20bn) increase in its administrative expenses due to a 314% surge in litigation claims to N6.52bn against the company.

As a result, Conoil recorded a decline in its profit before tax (PBT) and profit after tax (PAT) by 46.16% and 44.38% to N2.30bn and N1.58bn respectively. This was despite a 10.64% and 1227.11% increase in other operating income and other gains, a 21.27% decline in its distribution expenses and a 49.67% fall in income tax to N726.12mn in FY'17.

Conoil's profit was the least in the industry. Forte Oil had the highest PAT of N12.2bn with Total closely on its trail, with a PAT of N8bn in FY'17.

Taking into account its business segments, growth, cost management, and relative valuation, Conoil's current price is hovering around its intrinsic valuation. Accordingly, we place a **HOLD** rating on Conoil Plc.

Industry and Company Overview

The Nigerian oil and gas industry is the largest in Africa with an oil reserve of over 37.2bn barrels and a 197 trillion cubic feet gas reserve, the largest natural gas reserves in the continent. The Nigerian economy is highly dependent on oil as it accounts for 83% of export earnings and 9.61% of the GDP (Q1'18).

The Nigerian oil and gas industry is divided into three categories: the upstream, downstream, and services sector. The upstream sector involves searching for potential underground or underwater crude oil and natural gas fields. It includes drilling exploratory wells, and drilling and operating the wells that bring crude oil or raw natural gas to the surface. It is the most important sector in the economy as it accounts for over 83% of the country's exports. However, the upstream sector is vulnerable to asset vandalism. The last spike in vandalism was experienced in 2016. As a result, Nigeria's production declined to an all-time-low of 1.3mnbpd. In 2017, asset vandalism was minimal as the FG reached a ceasefire agreement with the militants.

The downstream sector deals mainly with the marketing and distribution of refined petroleum products from the refineries through pipelines, road trucks etc. The Petroleum Product Marketing Company (PPMC) supplies petroleum products in Nigeria to the oil marketers through a pipeline system that links the refineries to regional storage/sale depots.

Conoil Plc is the largest independent oil and gas company in Nigeria. It commenced operations in 1927 under the name Shell Trading Company. The company was incorporated in1960 as a private limited liability company under the name National Oil and Chemical Marketing Plc. In August 1991, it became a public limited liability company. The FGN held 40% of Shell Trading Company's shares until the privatization of the company, which led to the acquisition of 60% of the shares by Conpetro Ltd. Conpetro Ltd currently holds 74.4% of Conoil Plc while the remaining 25.6% is held by the general public.

Conoil Producing Ltd, the upstream arm, is the first indigenous company in Nigeria to explore, discover and produce oil in large commercial quantities. It is a leading oil and gas exploration and producing company well positioned in West Africa at large. Its principal activities include the exploration, production and sale of crude oil.

Table 1: Conoil Producing Ltd Operations

Petroleum Exploration

- Over 26 years exploration and production experience
- Operates six highly prospective oil blocks located in the Niger Delta region.

Petroleum Production

- Searches for new reserves in deeper formations of over 320 feet of net hydrocarbon sands in the oil prospecting lease (OPL) 290
- Field located in the south east shallow water, offshore Niger Delta.
- Its mobile offshore production unit has a daily capacity of 80,000bpd.
- Its oil seeps, natural gas seeps and pockmarks provide evidence of hydrocarbon generation.

Conoil Plc, the downstream arm, is a major petroleum marketing company involved in the sale of regulated kerosene and gasoline, diesel, aviation fuel and low pour fuel. It also manufactures and markets lubricants, chemicals and liquefied petroleum gas (LPG) for domestic and industrial use. The company operates through three business categories: white products, lubricants, and LPG. Table 2 shows an overview of the company's different business units.

Table 2: Conoil Plc Business Operations

S/N	Business Segment	Overview
1.	White Product	• Involved in the sale of premium motor spirit (PMS), automotive gasoline/grease oil (AGO), dual purpose kerosene (DPK), aviation turbine kerosene (ATK) and low-pour fuel oil (LPFO) to retail and industrial customers. • It has over 1,200 retail outlets across Nigeria. • Conoil is the leader of development in modern retail outlets such as mega stations and non-space pumps.
2.	Lubricants	• Responsible for the sale of lubricants for transport and industrial use, greases, process oil and bitumen. • Key product brands include Quatro and Golden Super Motor Oil.
3.	LPG	• Manufactures and sells LPG through cylinders and valves.

The company's retail has grown an expansive distribution network throughout the country to ensure its customers get value and satisfaction through its quality products. Its distribution is done through its own network of branches, dealers and distribution spread. Conoil currently has 395 dealers and distributors across Nigeria. Its major supplier of white products remains the NNPC.

The dominant players in the upstream sector include Oando and Seplat, while the dominant players in the downstream arm include Total, Forte Oil, 11Plc and Chevron.

Conoil's financial results reflect its growth performance.

Income Statement for Conoil Oil Plc (FY Dec 2017)					
N'000	**2013**	**2014**	**2015**	**2016**	**2017**
Revenue	159,537,133	128,352,674	82,919,220	85,023,546	115,513,246
Cost of Sales	(142,498,615)	(114,563,202)	(71,381,463)	(70,882,997)	(102,463,874)
Gross Profit	17,038,518	13,789,472	11,537,757	14,140,549	13,049,372
Other Operating Income	2,758,537	173,437	2,718,438	2,280,235	2,522,765
Distribution Expenses	(4,529,495)	(2,728,155)	(2,697,837)	(2,534,598)	(1,995,504)
Administrative Expenses	(8,391,204)	(8,155,991)	(6,885,734)	(7,995,977)	(11,195,005)
Other Gains/Losses	(48,706)	761,178	2,533,281	155,237	2,060,169
Finance Cost	(2,251,826)	(2,307,767)	(3,757,508)	(1,764,897)	(2,137,170)
Profit Before Tax	4,575,824	1,532,174	3,448,397	4,280,549	2,304,627
Income Tax Expense	(1,505,733)	(697,753)	(1,140,840)	(1,442,665)	(726,120)
Profit for the Year (PAT)	3,070,091	834,421	2,307,557	2,837,884	1,578,507

Balance Sheet for Conoil Oil Plc (FY Dec 2017)					
N'000	**2013**	**2014**	**2015**	**2016**	**2017**
Property, Plant & Equipment	4,833,632	3,927,386	3,169,460	2,438,467	2,519,941
Investment Property	496,500	446,850	397,200	347,550	297,900
Intangible Assets	95,522	84,908	74,294	63,680	53,066
Other Financial Assets	10	10	10	10	10
Prepayments	245,566	100,359	97,104	163,045	199,485
Deferred Tax Assets	-	1,599,035	1,994,988	2,749,942	2,412,680
Non-current Assets	5,671,230	6,158,548	5,733,056	5,762,694	5,483,082
Inventories	10,635,426	5,516,195	5,550,287	5,255,596	5,661,155
Prepayments	160,889	246,004	189,116	135,890	69,230
Trade and Other Receivables	38,117,934	44,447,855	28,024,348	16,383,929	25,866,860
Cash and Cash Equivalent	27,786,547	31,158,085	29,890,557	42,295,355	25,774,757
Current Assets	76,700,796	81,368,139	63,654,308	64,070,770	57,372,002
Total Assets	82,372,026	87,526,687	69,387,364	69,833,464	62,855,084
Share Capital	346,976	346,976	346,976	346,976	346,976
Share Premium	3,824,770	3,824,770	3,824,770	3,824,770	3,824,770
Retained Earnings	13,865,688	11,924,301	13,537,907	14,293,935	13,721,190
Total Equity	18,037,434	16,096,047	17,709,653	18,465,681	17,892,936
Deferred Tax Liabilities	352,910	933,230	693,515	428,693	365,773
Distributor's Deposits	496,397	498,347	501,697	502,859	496,610
Decommissioning Liability	27,669	32,511	38,200	52,141	54,616
Non-current Liabilities	876,976	1,464,088	1,233,412	983,693	916,999
Borrowings	11,828,937	22,655,108	18,235,913	8,990,872	5,178,802
Bank Overdrafts	-	-	-	-	-
Current Income Tax Liabilities	2,826,206	3,770,483	3,348,544	4,034,453	2,293,116
Trade and Other Payables	48,802,473	43,540,961	28,859,842	37,358,765	36,573,231
Current Liabilities	63,457,616	69,966,552	50,444,299	50,384,090	44,045,149
Total Liabilities	64,334,592	71,430,640	51,677,711	51,367,783	44,962,148
Total Equity and Liabilities	82,372,026	87,526,687	69,387,364	69,833,464	62,855,084

[21]

[21] Source: Conoil Plc Financial Statements

Management

Seasoned professionals determined to grow in a tough operating environment

Conoil Nigeria's growth over the years can be attributed to its management team with a wide range of experience in the petroleum industry. Mr. Mike Adeniyi Adenuga is the Chairman of the Board of Directors. He has founded and nurtured many energy, oil and gas, banking (Devcom Bank and Equatorial Trust Bank (now Sterling Bank)), telecommunication (Glo) and real estate businesses into profitable companies. He was awarded with Grand Commander of the Order of the Niger (GCON) and the Companion of the Star of Ghana, (CSG).

Mr. Pandey Ajay is the acting Managing Director effective 2017. He is a seasoned management professional with over 24-years experience. He has an enviable record of steering new initiatives and impacting organizations across their top and bottom-line, their corporate strategic planning, and their process, performance, profit and loss, and acquisition management. He has expertise in new product launches such as lubricants (Elf, Total, Relstar, Conoil Plc, Masters Lubricants) and LPG (Congas and Masters Gas, Diamond Petro Lubes), distribution network appointment/development, supply and distribution, product pricing and multi-channel management, leadership and decision making as well as monitoring and evaluating performances.

Downstream companies in Nigeria have been largely affected by the significant fall in global oil prices since 2014, the advancement in shale oil production techniques and weak global economic growth. Despite major divestments of integrated oil and gas companies, and the tough operating environment in the Nigerian downstream sector, Conoil Plc has continued to make significant investments, demonstrating its long-term strategy and commitment to the downstream oil sector. Conoil's growth is sustainable due to steady improvements in its earnings and shareholders' returns.

Chairman of the Board of Directors

Mr. Mike Adeniyi Adenuga

Managing Director

Mr. Pandey Ajay

The Bull and the Bear Says:

- Leading indigenous brand in the oil and gas industry
- Reputable brand in the Nigerian downstream sector
- Talented and well experienced management
- Wide range of top quality products and services
- Extensive distribution network

- Intense competition from other leading petroleum marketers such as 11 Plc, Oando and Forte Oil Plc
- Persistent foreign exchange challenges
- Delay in the passage of the Petroleum Industry Bill (PIB)
- Volatility in the price of petroleum products can threaten its revenue stream
- Threat of the resurgence of insecurity in the Niger -Delta

Risk and Outlook

Great opportunities with probable macroeconomic and competitor headwinds

Conoil Plc is exposed to risks such as market (currency and interest rate risks), credit and liquidity risks amid corporate governance risk. These risks could prevent Conoil from expanding in the downstream space to improve market leadership. The company assigns risk management roles at three levels: the Board through the Board Risk and Management Committee, Executive Committee through the Executive Management Committee and Line Managers who manage risk exposures that occur from daily operations.

Conoil borrows funds at both fixed and floating interest rates and as a result is exposed to high interest-bearing debts. The company mitigates this risk by maintaining an appropriate mix between its short term and long term borrowings, and negotiating with its banks to ensure rates are consistent with the Central Bank of Nigeria's (CBN) monetary policy rate (MPR).

The company's foreign transactions are predominantly in US dollars, which exposes it to exchange rate volatility. In addition, increased pressure on the naira could affect product supply and increase its finance costs, which will adversely affect bottom-line earnings. Conoil currently controls this risk by managing exchange rate exposures within the approved policy parameters by utilizing forward foreign exchange contracts.

The company is exposed to liquidity risks, which implies that suitable sources of funding for business activities may not be available. As a result, the company has a liquidity risk management framework that manages its short, medium and long term funding.

Conoil mitigates this risk by maintain reserves, banking facilities and reserve borrowing facilities. In addition, it monitors forecast and actual cash flows by maintaining maturity profiles of financial assets and liabilities. The company predominantly deals with only credit worthy counterparties and obtains sufficient collateral when necessary to mitigate the risk of financial loss.

The removal of fuel subsidies in 2016 is a major reform that positively impacts sales and earnings. However, it also adds pressure to consumer costs. This is in addition to the weak labor dynamics plaguing the Nigerian economy. The current shift in the market to value products could lead to a reduced demand for fuel products as an increasing number of people use public transportation.

Other oil and gas companies in Nigeria are actively seeking ways of increasing market share and earnings. Oando Plc, one of its competitors, divested from three business segments: energy services, gas and power, and marketing, refining and terminal segments. It did so to focus on its up-and-mid stream segments. Oando, in 2014, acquired ConocoPhillips and recently embarked on a tripartite agreement with Vitol, the world's largest independent trader of energy commodities, and Helios Investment Partners to strengthen its aim of becoming a dominant player in the upstream sector. This poses a significant threat to Conoil as Oando has the potential to decrease its market share.

OUR valuation

We derived our valuation for Conoil Plc by using the Discounted Cash Flow (DCF) methodology. Our fair value estimate for Conoil stood at **N25.50**, which is an 8.93% upside on its current share price of N28.00 as of July 11, 2018. The discount rate [weighted average cost of capital (WACC)] of 19% is derived using a 13.5% risk free rate [the yield for a 10-year Federal Government of Nigeria (FGN) bond maturing in March 2027], a beta of 0.9340, an after-tax cost of debt of 11.9%, and a market risk premium of 6.4%. The calculated long-term cash flow growth rate to perpetuity is 5%.

[22]Financial Times Data