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OIL PRICES: THE SAUDI CHESS GAME

Early this year, with its sights set on a $2 trillion (trn) valuation for its state oil company, Saudi ARAMCO, ahead of a planned initial public offering (IPO), Saudi Arabia was doing all it could to push oil prices to $100 per barrel (pb). Oil prices were rising faster than anyone anticipated. The US announced a return of sanctions on Iran – including its oil exports – beginning in November. The anticipated shortfall from a removal of 1.4 million barrels per day (mbpd) of Iranian oil from the market put even more upward pressure on oil prices. Compliance levels to the pact between the Organization of the Petroleum Exporting Countries (OPEC) and non-OPEC oil producers to curb output exceeded 100%. Venezuela's production continued to plunge by around 40,000bpd monthly while production shut-ins in Libya and Nigeria persisted. The coalition's objective of oil market re-balancing was looking increasingly like "mission accomplished", to the surprise of naysayers and skeptics, as oil hit $80pb in May for the first time since the end of 2014.

For the Saudis, the world's largest IPO ($100bn) was seemingly in the cards as there seemed to be no stopping the oil surge. Fast-rising prices were creating unhappy customers in large oil-importing nations across the globe. This was until US President Donald Trump apparently had enough. With his sights seemingly set on the US mid-term elections in November, and the damage high gasoline prices could do, President Trump went on twitter and berated OPEC for keeping gas prices "artificially high".

Between a rock and a hard place

This was enough to nudge the OPEC/non-OPEC coalition into a re-think. In June, they agreed to ease compliance rates and raise output by 1mbpd. The Saudis, in response to Trump's vocal expression of displeasure at OPEC, led the move. They have been fervent supporters of Trump's policy towards Iran while the Saudi-US diplomatic alliance has strengthened under Trump.

The Saudi ARAMCO IPO has since been called off but that is not the only reason they needed high oil prices. Achieving widely advertised economic reforms under its Vision 2030 program also requires that oil prices stay high. The dilemma the Saudis are currently confronted with is managing the oil market in a way that balances its fiscal needs with its need to strengthen diplomatic ties with the US. The Saudis appear to want prices high – between the $70pb-$80pb band – but not high enough to get on Trump's nerves and threaten the increasingly cordial ties with the US Administration under President Trump.

But for how long?

Lower gasoline prices ahead of the mid-term elections scheduled for November 6th appear to be on Trump's agenda. So, does this agenda change after the mid-terms? Do Saudi Arabia and OPEC automatically have the go-ahead to return to their initial strategy of limiting output to achieve a more desirable price level? Will it no longer bother Trump if OPEC makes gas prices "artificially high"? These are just a few of the questions being asked by analysts. As sanctions on Iran take effect, offsetting the reduction in global oil supply will require action on the part of the OPEC/non-OPEC coalition if $70-80pb prices are to be maintained. Given that some countries are unable to pump more, Saudi's spare capacity is likely to come in to play – about 1.7mbpd.[1] This is in addition to the sale of 11 million barrels of oil from the Strategic Petroleum Reserve in November, already authorized by Trump.

[1]Tsvetana Paraskova, September 4, 2018. "Saudi Aramco signs deal with Baker Hughes to boost offshore oil production", Oilprice.com, https://oilprice.com/Latest-Energy-News/World-News/Saudi-Aramco-Signs-Deal-With-Baker-Hughes-To-Boost-Offshore-Oil-Production.html

Intent from the on-set

Without jettisoning its objective, the OPEC/non-OPEC coalition recognizes the possible negative impact of higher prices on demand. They have boosted production to ease concerns about high prices and expected losses from Iran and Venezuela. The Saudi's have specifically targeted increased exports to the US – the world's most transparent market – which reports crude oil imports and inventory levels weekly. This move is strategic as the reports typically have a significant influence on the price of oil and investor sentiment.

Data from the Energy information Administration (EIA) showed that US oil imports from Saudi Arabia surpassed 1mbpd[2] for the first time since June 2017. This is after cutting crude shipments to the US down to a 30-year-low when they were neck-deep in their quest for oil market rebalancing. As OPEC's leader and largest producer, their intention was to have reports of their reduction in exports to the US impact positively on oil prices and investment sentiment – which it did.

By the end of October 2017, the 4-week average of Saudi Arabia's exports to the US had fallen to 506,000bpd – the lowest level since late 1987. This is roughly half of the four-week average of 1.009mbpd for the last week of August this year. The Saudi-controlled Motiva refinery – the largest in the US, with a 600,000bpd capacity – has begun to increase imports of Saudi oil again after cutting down on them last year when more Iraqi oil was imported in the past year.[3] US oil imports from Saudi Arabia in September and October of 2018 are poised to reach the highest two -month level since February and March 2017 – estimated at 41.5 million barrels of oil.[4]

The End Game

The Saudis intend to regain market share and quell bullish oil market sentiment – at least for now. After the US mid-term elections in November, they could decide to not touch their spare capacity and watch market dynamics play out. Iranian exports going offline could mean oil prices rising to somewhere around $90pb. That may dent demand, but it is a game the Saudis are more than willing to play unless Trump wades in.

[2]Independent Statistics & Analysis, "4-week average imports from Saudi Arabia of crude oil." US Energy Information Administration. https://www.eia.gov/dnav/pet/hist/LeafHandler.ashx?n=pet&s=w_epc0_im0_nus-nsa_mbbld&f=4

[3]Javier Blas, September 7, 2018. "In response to Trump, Saudis ramp up oil exports into the US", Bloomberg, https://www.bloomberg.com/news/articles/2018-09-07/in-response-to-trump-saudis-ramp-up-oil-exports-into-the-u-s

[4]Collin Eaton, September 6, 2018. "Saudi crude exports to US jump as it moves to recapture share," Reuters. https://www.nasdaq.com/article/saudi-crude-exports-to-us-jump-as-it-moves-to-recapture-share-20180906-01022

NIGERIA'S PERFORMANCE ON THE MILLENNIUM DEVELOPMENT GOALS:

A LESSON FOR THE SUSTAINABLE DEVELOPMENT GOALS

In 2000, the United Nations member states met to discuss ways to fight world poverty in its various dimensions. The conclusion of this meeting translated to the eight Millennium Development Goals (MDGs), which were to be carried out by the member states over the next decade and a half. The goals were:

- Eradicate extreme poverty and hunger
- Achieve universal primary education
- Promote gender equality and empower women
- Reduce child mortality
- Improve maternal health
- Combat HIV/AIDS, malaria, and other diseases
- Ensure environmental sustainability
- Develop a global partnership for development

By the target date, 2015 end, there was reason to celebrate as significant progress had been made across all goals and the MDGs were even hailed as the most successful anti-poverty movement in history.[5] However, in Nigeria, the same could not be said. Six out of the eight goals were not achieved, according to the Nigeria 2015 Millennium Development Goals End Point report. Global attention has now turned to the Sustainable Development Goals (SDGs), which are a universal call to end poverty, protect the planet and ensure that all people enjoy peace and prosperity.

[5]World Federation of Engineering Organisations.n.d."The Final Report of the MDGs". http://www.wfeo.org/final-report-mdgs/.

They are meant to build on the successes of the MDGs. In order for Nigeria to be able to successfully implement and achieve the global SDGs, it has to first identify where it fell short of achieving the MDGs. By looking into the shortcomings in achieving the MDGs "eradicate extreme poverty and hunger" and "combat HIV/AIDS and other diseases", we can better understand how Nigeria can approach and achieve the SDGs "no poverty", "zero hunger", and "good health and well-being" by the target date 2030.

MDG 1: Eradicate extreme poverty and hunger

According to the United Nations Millennium Development Goals report, significant progress was made globally with respect to achieving this goal

- In 1990, almost 50% of the population in the developing world lived on less than $1.25 per day and that proportion fell to 14% in 2015.
- The number of people living in extreme poverty declined by more than 50% from 1.9 billion in 1990 to 836 million in 2015.
- The proportion of undernourished people in developing economies dropped by almost half since 1990, from 23.3% between 1990 – 1992 to 12.9% in 2014 – 2016.[6]

While success was recorded on the global front, Nigeria made a paltry attempt.

Target: Reduce the proportion of people living in extreme poverty by 50% between 1990 and 2015	
Indicator	***Progress***
Proportion of population below $1 per day	Weak (<45% of target met)
Poverty gap ratio	Fair (45% - 59% of target met)
Share of poorest quintile in national consumption	Fair (45% - 59% of target met)
Target: Halve, between 1990 and 2015, the proportion of people who suffer hunger	
Prevalence of underweight children under-five years of age	Fair (45% - 59% of target met)[7]

[6]United Nations. 2015. "The Millennium Development Goals Report".
http://www.un.org/millenniumgoals/2015_MDG_Report/pdf/MDG%202015%20rev%20%28July%201%29.pdf
[7]OSSAPMDG. 2015. "Nigeria 2015 Millennium Development Goals End-Point Report".
http://www.undp.org/content/dam/undp/library/MDG/english/MDG%20Country%20Reports/Nigeria/Nigeria_MDGs_Abridged_Sept30.pdf

The gap in these targets was particularly concentrated in the northern states and rural areas where there remains a high prevalence of hunger.[8]

MDG 6: Combat HIV/AIDS, malaria, and other diseases

The MDGR 2015 states:

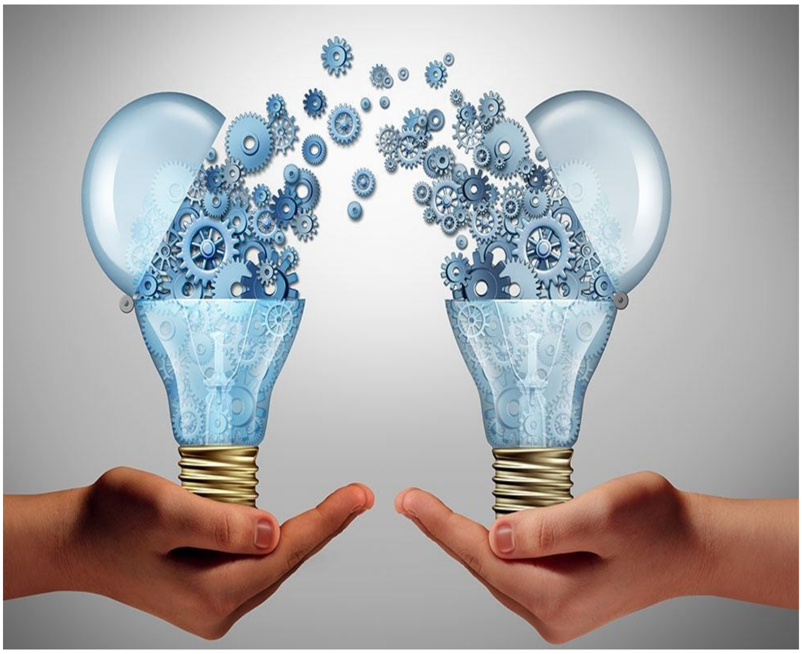
- Globally, the number of new HIV infections fell by about 40% from 3.5 million to 2.1 million between 2000 and 2013.
- By June 2014, 13.6 million people living with HIV were receiving antiretroviral therapy (an increase from 800,000 in 2003), averting 7.6 million deaths from AIDS between 1995 and 2013.
- Nearly 37 million lives were saved due to tuberculosis prevention, diagnosis and treatment interventions between 2000 and 2013. This decreased the tuberculosis mortality rate by 45% and the prevalence of the disease by 41% between 1990 and 2013.

The progress made by Nigeria in combating HIV/AIDS and other diseases are summarized in the following table.

Target: To stop the spread of HIV and AIDS by 2015	
Indicator	***Progress***
HIV prevalence among pregnant young women aged 15 – 24years	Weak (<45% of target met)
Proportion of the population with advanced HIV infection with access to antiretroviral drugs	Weak (<45% of target met)
Target: To stop the incidence of malaria and other major diseases by 2015	
Incidence, prevalence and death rates associated with tuberculosis	Weak (<45% of target met)
Incidence and death rates associated with malaria	Strong (>60% of target met)[9]

[8]OSSAPMDG. 2015. "Nigeria 2015 Millennium Development Goals End-Point Report". http://www.undp.org/content/dam/undp/library/MDG/english/MDG%20Country%20Reports/Nigeria/Nigeria_MDGs_Abridged_Sept30.pdf
[9]OSSAPMDG. 2015. "Nigeria 2015 Millennium Development Goals End-Point Report". http://www.undp.org/content/dam/undp/library/MDG/english/MDG%20Country%20Reports/Nigeria/Nigeria_MDGs_Abridged_Sept30.pdf

With respect to tuberculosis as of 2005, 343 people per 100,000 had the disease in Nigeria. By 2012 that number had only decreased by four to 339, and by 2013 it had decreased by only one to 338.[10] Clearly, the country did not significantly contribute to the global progress recorded by the UN. A key reason was lack of uptake in the north as there is a long-held belief in some areas of the north that vaccines kill children.[11]



Lessons from other countries

Most of the countries in the Asia-Pacific region were key drivers in the global progress of the MDGs because their governments clearly set goals and incorporated the MDGs' framework into their national development planning.[12] A good example is Armenia. The country made appreciable progress in the achievement of MDG 1 (eradicate extreme poverty and hunger). A contributor to this was the economic growth of 3.5% recorded in 2013 and an increase in its tax revenues by 21% to $1.2bn in the first half of that year.[13] These enabled the government to raise the minimum wage rate to $108/month from $84/month, moving many above the poverty line.[14] A way to learn from Armenia would be to adopt short-term policies that would encourage consumer consumption, which would boost expenditure and encourage production, hence raising the growth rate. This would then allow the government to review the minimum wage rate and consider raising it to improve the standard of living provided that there is a rise in government revenue.

[10]OSSAPMDG. 2015. "Nigeria 2015 Millennium Development Goals End-Point Report". http://www.undp.org/content/dam/undp/library/MDG/english/MDG%20Country%20Reports/Nigeria/Nigeria_MDGs_Abridged_Sept30.pdf

[11]Ajiye, S. 2014. "Achievements of Millennium Development Goals in Nigeria: A Critical Examination". Institute for Peace and Conflict Resolution. https://pdfs.semanticscholar.org/7767/ec3ba825462626217a63ad8806e1eda687f2.pdf

[12]ADB, UN ESCAP, UNDP. 2015. "Making It Happen: Technology, Finance, and Statistics for Sustainable Development in Asia and the Pacific". http://www.undp.org/content/dam/rbap/docs/Research%20&%20Publications/mdg/RBAP-RMDG-Report-2014-2015.pdf

[13]EIU. 2013. "Tax revenue rises rapidly". http://country.eiu.com/article.aspx?articleid=150895199&Country=Armenia&topic=Economy&subtopic=Fo_2

[14]UNDP. 2018. "Armenia: Poverty Reduction". http://www.am.undp.org/content/armenia/en/home/ourwork/povertyreduction/overview.html

With respect to MDG 6, which was to achieve universal access to treatment for HIV/AIDS for all who need it, key contributors to the goal were Cambodia, Fiji, Botswana, Namibia, and Rwanda. These countries contributed to this goal by making efforts to provide access to antiretroviral therapy, and were able to do so to about 80% of the people that needed it.[15] Cambodia was also successful in combating tuberculosis. The country launched a national tuberculosis program, and with support from international organizations, was able to provide the required care at the grass-roots level of the country.[16]

With regards to HIV/AIDS and other diseases, a national survey could be carried out, like Cambodia did in 2002 for tuberculosis prevalence, to locate the areas where such diseases are concentrated and subsequently focus government efforts.[17] This would go a long way in reducing the prevalence of such diseases.

These tactics can be adopted in Nigeria in order to meet the SDGs provided that consistent efforts are made to eliminate problems such as corruption in political offices and the Boko Haram insurgency that is plaguing the country. The government can also streamline the goals into its policies and the national budget, as well as enlighten the public on the goals and its efforts to achieve them. Making the public understand the goals and their potential impact on society can help drive public support for government efforts like vaccinations, other public health initiatives and economic programs put in place to achieve the goals.

[15]United Nations. 2013. “The Millennium Development Goals Report 2013”.
[16]United Nations. 2013. “The Millennium Development Goals Report 2013”.
[17]United Nations. 2013. “The Millennium Development Goals Report 2013”.

WHAT OIL AT $100 A BARREL WOULD MEAN FOR THE GLOBAL ECONOMY

Global Perspective - Culled from Bloomberg

Rising oil prices are prompting forecasts of a return to $100 a barrel for the first time since 2014, creating both winners and losers in the world economy.

Exporters of the fuel would enjoy bumper returns, giving a fillip to companies and government coffers. By contrast, consuming nations would bear the cost at the pump, potentially fanning inflation and hurting demand.

The good news is that Bloomberg Economics found that oil at $100 would mean less for global growth in 2018 than it did after the 2011 spike. That's partly because economies are less reliant on energy and because the shale revolution cushioning the U.S.

Ultimately, much depends on why prices are pushing higher. A shock amid constrained supply is a negative, but one due to robust demand just reflects solid growth. Both forces are now in play, driving Brent crude up about 22 percent this year.

What does it mean for global growth?

Higher oil prices would hurt household incomes and consumer spending, but the impact would vary. Europe is vulnerable given that many of the region's countries are oil importers. China is the world's biggest importer of oil and could expect an uptick in inflation.

There are also seasonal effects to consider, with winter looming in the Northern hemisphere. Consumers can switch energy sources to keep costs down, such as biofuels or natural gas, although not quickly. Indonesia already has instituted measures to push more use of biofuels and limit the economy's reliance on imported fuel.

For a sustained hit to global growth, economists say oil would need to hold above $100. The dollar's gain of this year doesn't help though given crude is priced in greenbacks.

How can the world economy absorb oil at $100?

Bloomberg Economics found that $100 oil will do more harm than good to global growth. Yet there are important differences in the condition of the world economy today compared with 2011.

"The shale revolution, lower energy intensity, and higher general price levels mean the impact will be smaller than it once was," economists led by Jamie Murray wrote in a recent report. "The price of a barrel will have to go much higher before global growth slips on an oil slick."

How will Iran and Trump impact the market?

Geopolitics remains a wild card. Renewed U.S. sanctions on Iran are already crimping the Middle East nation's oil exports. While President Donald Trump is pressuring the Organization of Petroleum Exporting Countries to pump more, there is limited spare production capacity. In addition, supply from nations including Venezuela, Libya and Nigeria is being buffeted by economic collapse or civil unrest. Still, Goldman Sachs analysts predict $100 will not be passed.

Who wins from higher oil prices?

Most of the biggest oil-producing nations are emerging economies. Saudi Arabia leads the way with a net oil production that's almost 21 percent of gross domestic product as of 2016 -- more than twice that of Russia, which is the next among 15 major emerging markets ranked by Bloomberg Economics. Other winners could include Nigeria and Colombia. The increase in revenues will help to repair budgets and current account deficits, allowing governments to increase spending that will spur investment.

Who loses?

India, China, Taiwan, Chile, Turkey, Egypt and Ukraine are among the nations who would take a hit. Paying more for oil will pressure current accounts and make economies more vulnerable to rising U.S. interest rates. Bloomberg Economics has ranked major emerging markets based on vulnerability to shifts in oil prices, U.S. rates and protectionism.

One of the biggest winners might also find itself on the losing end: Oystein Olsen, Norway's central bank governor, warned that western Europe's biggest petroleum producer risks problems if the industry takes its eyes off controlling costs.

What does it mean for the world's biggest economy?

A run-up in oil prices poses a lot less of a risk to the U.S. than it used to, thanks to the boom in shale oil production. The old rule of thumb among economists was that a sustained $10 per barrel increase would shave about 0.3 percent off of U.S. output the following year. But tallies now, including that of Moody's Analytics chief economist Mark Zandi, pencil in a hit of around 0.1 percent.

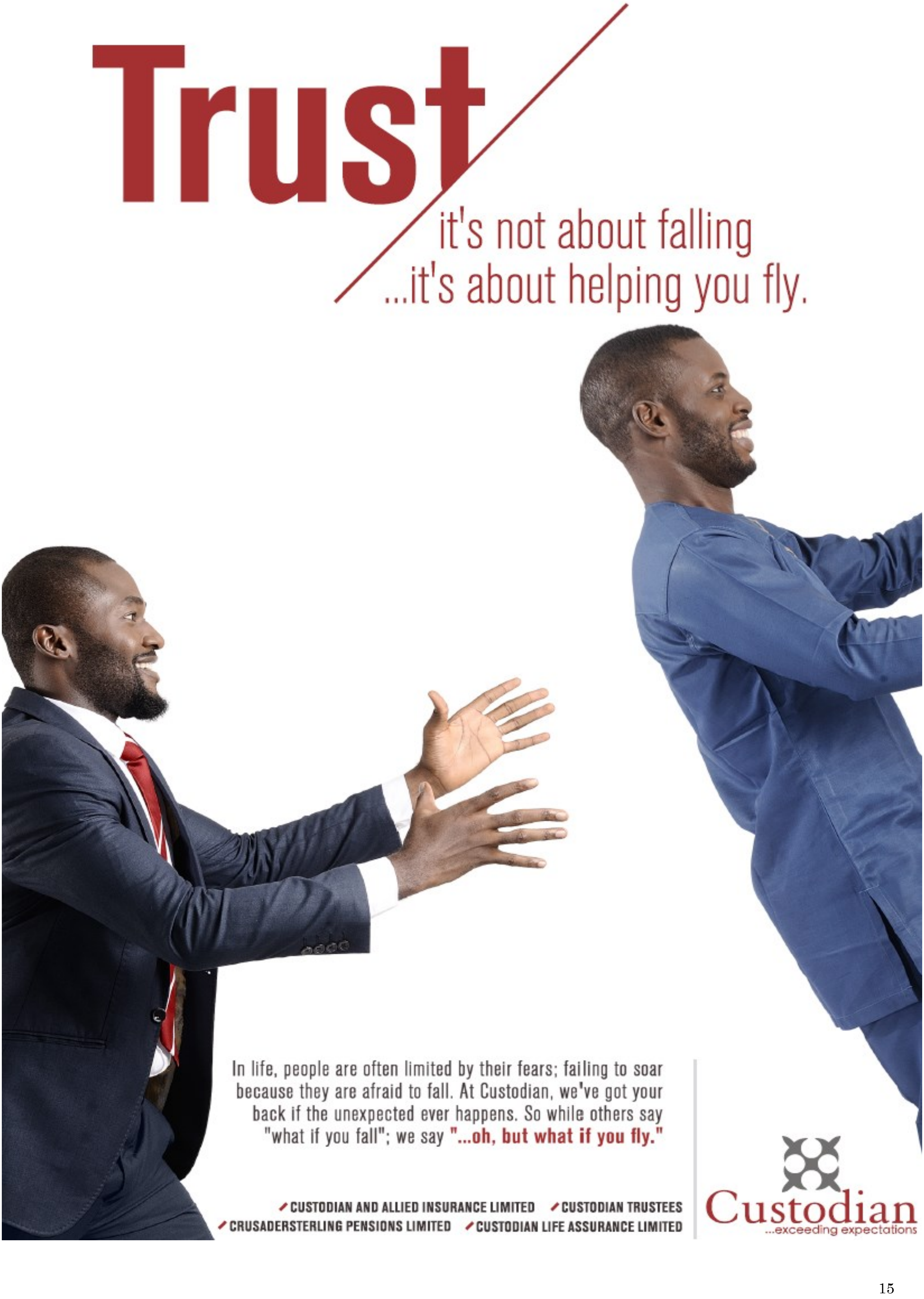
While the diminishing American reliance on imported oil has positive economic consequences at the industry level, poorer households would feel the weight of higher prices at the pump. They spend about 8 percent of their pre-tax income on gasoline, compared to about one percent for the top fifth of earners.

Will it lead to higher inflation around the world?

Energy prices often carry a heavy weight in consumer price gauges, prompting policy makers including those at the Federal Reserve to focus simultaneously on core indexes that remove volatile energy costs. But a substantial run-up in oil prices could provide a more durable uptick for overall inflation if the costs filter through to transportation and utilities.

What does it mean for central banks?

If stronger oil prices boost inflation, central bankers on balance will have one less reason to keep monetary policy loose. Among the most-exposed economies, central bankers in India already are warning about the impact as the nation's biggest import item gets more expensive. Greater overall price pressures also could prompt faster monetary policy tightening in economies such as Thailand, Indonesia, the Philippines and South Africa.


Trust
it's not about falling
...it's about helping you fly.
In life, people are often limited by their fears; failing to soar because they are afraid to fall. At Custodian, we've got your back if the unexpected ever happens. So while others say "what if you fall"; we say "...oh, but what if you fly."
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CUSTODIAN LIFE ASSURANCE LIMITED
Custodian
...exceeding expectations

NIGERIA'S FUEL SUBSIDIES BILL SET TO SOAR ON RISING OIL PRICE

Global Perspective - Culled from the Financial Times

Rising crude oil prices are set to send Nigeria's bill for fuel subsidies rocketing, threatening to exacerbate the already precarious economic situation of Africa's largest oil producer as it heads into election season.

Although Nigeria produces 1.7m barrels of crude per day, it has very little refining capacity and imports roughly 90 per cent of its fuel, negating much of the benefits oil-producing nations accrue from high crude prices.

When crude prices plunged to about $30 a barrel in 2016, it sent Nigeria's oil-dependent economy reeling into a recession from which it has barely recovered. While a rally has since pushed the oil price past $85, Africa's most populous country is not set to reap the benefits. This is because its subsidy bill is likely to surge beyond the $3.85bn annual tally the oil minister estimated earlier this year when prices were 20 per cent lower, said Tunde Ajileye, a partner at SBM Intel, a political and economic risk consultancy.

"We sit on a double-edged sword: when oil prices go down, government revenues go down and it becomes difficult to get foreign exchange," he said. "When oil prices go up, while there is usually an increase in government revenues . . . the big issue is that for refined products like fuel and diesel, the prices go up and [then] . . . the subsidy bill goes up."

In April, when crude averaged about $70 a barrel, Emmanuel Kachikwu, the oil minister, reportedly said the annual fuel subsidy bill had risen to 1.4tn naira ($3.85bn) — that is roughly half the N2.67tn the government collected in net oil revenues in 2017 or a quarter of total net government revenues that year.

That month, the Nigerian National Petroleum Corporation paid roughly $215m in what it calls "under-recovery" costs: the difference between what it paid to import fuel and how much it sells the fuel for. In May, when Brent crude prices averaged about $77, NNPC paid $245m to fill the gap.

With oil prices now 10 per cent higher and climbing, that bill is set to soar, creating a predicament for the government ahead of February's elections, said Mr Ajileye. The outlay is unsustainable, he said.

"The government has to make a decision of whether to increase fuel prices domestically," he said. "That's a very politically charged issue."

The last time a government in Nigeria tried to scrap the subsidy altogether, in 2013, it prompted widespread protests.

Nigeria has the potential to produce more than 2.5m barrels a day. But it rarely reaches that level because of poor infrastructure, theft and pipeline sabotage driven by unrest in the oil-rich Niger Delta region. State-run refineries operate at less than 10 per cent of their 445,000 barrel-a-day capacity. The government then sells the fuel to retailers, which sell on to the public at the subsidised rate of N145 a litre.

Crude accounts for 56 per cent of government revenues, while the country's annual fuel import bill tops $7bn.

As part of a reform the government said was aimed at cleaning up the corruption-addled subsidy regime, President Muhammadu Buhari, in effect, turned state-run NNPC into the country's sole fuel importer, cutting out private sector middlemen marketers.

That has increased the potential for graft within the NNPC, a longstanding cash cow for the government, particularly in the run-up to elections, said Jubril Kareem, an energy analyst at Ecobank.

“NNPC is just too big a company, and the opaqueness of the operations is actually aided by its own structure: it produces crude, buys crude, sells fuel, it regulates itself,” he said. “At least before, we knew what NNPC was paying in subsidy [because of monthly reports that the NNPC no longer regularly issues]. Now you don’t know that . . . You would understand why a government would want to keep it that way.”

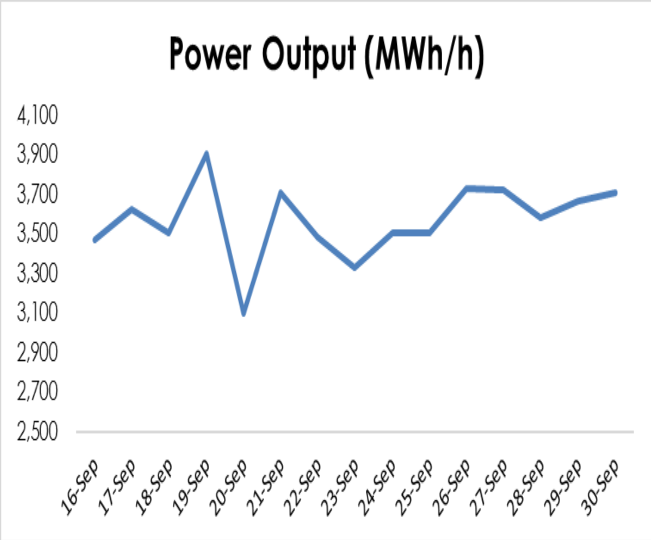
Fuel subsidies have long been the subject of abuse and corruption. They also encourage smuggling into neighbouring Cameroon and Benin, where fuel can be sold for twice the price, and even more as international oil prices rise.

A former central bank governor has estimated that more than $1bn went missing every month from oil sales and fuel subsidy scams during a single 19-month period between January 2012 and July 2013 that he examined. He was subsequently sacked.

MACROECONOMIC INDICATORS

Power Sector

The average power output from the national grid was 3,570MWh/h within the period of 16th – 30th September. This is 2.62% lower than the average of 3,666MWh/h in the corresponding period in August. The decline resulted from the gas constraints that occurred during the period especially from Afam VI, Geregu NIPP, and Odukpani NIPP. The sector lost a total of N24.55bn during the period.



[18]

Outlook

Hydro-generated power is expected to increase in the coming weeks if the intense rainfall persists. However, power output has been on the decline despite the intense rains, implying that supply would depend largely on gas.

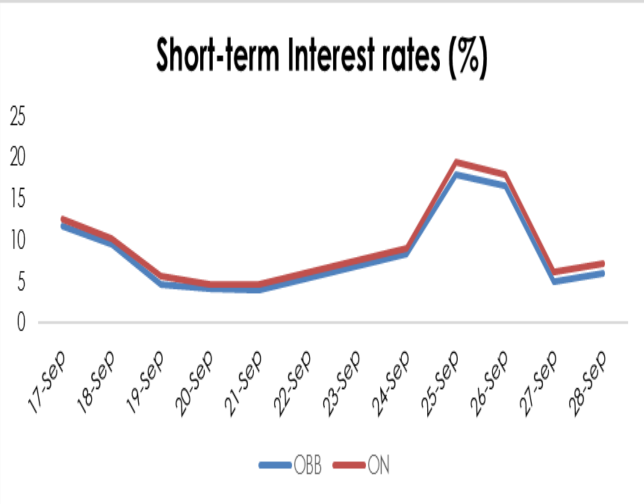
Money Market

Average opening position for banks was N361.50bn between September 17th – 28th, compared to N333.42bn in the corresponding period in August. Total OMO sales during the period was N337.60bn compared to maturities of N479.41bn, this resulted in a net inflow of N141.81bn. Average NIBOR (OBB, O/N) was 9.31% pa within the review period, compared to 10.49% pa in the corresponding period in August.

At the primary market auction on September 19th, the 91-day T/Bills remained flat, while the 182-day and the 364-day T/Bills declined. At the secondary market, the three tenors declined.

Tenor	Primary market (September 12th, 2018) (%)	Primary market (September 19th, 2018) (%)	Secondary market (September 17th, 2018) (%)	Secondary market (September, 28th 2018) (%)
91-day	11.00	11.00	13.08	12.35
182-day	12.30	12.20	13.68	12.39
364-day	13.50	13.48	13.57	13.46

[18] FGN



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Outlook

We expect a fall in interest rates in the near term following the surge in money supply due to pre-election spending and the FAAC disbursement. Higher oil export proceeds and a possible review of the minimum wage would further support this trend.

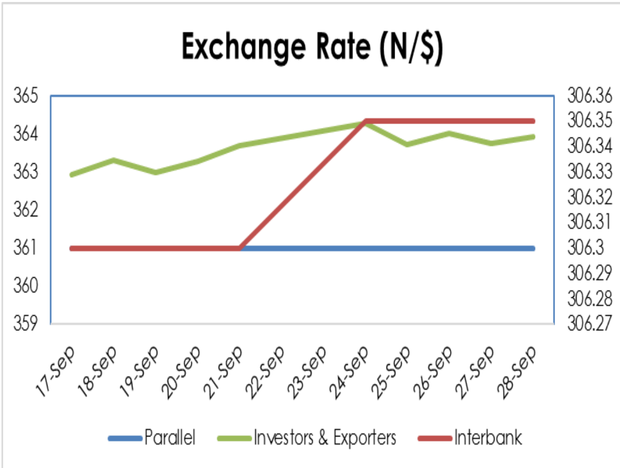
Forex Market

Exchange Rate

At the parallel market, after 20 days of horizontal trading at N361/$, the naira depreciated by 0.28% to close at N362/$ on October 12th. At the interbank foreign exchange market, the naira depreciated marginally by 0.02% to close the period at N306.45/$, from N306.40/$ on October 2nd. The naira also depreciated by 0.07% to close at N364.12/$ at the IEFX window from N363.88/$ on October 2nd. The currency has depreciated below the parallel market rate, partly due to increased capital reversal. Total forex traded at the IEFX window in the period was $2.95bn, compared to $3.09bn in the corresponding period in August.

Outlook

The naira was relatively stable during the period as a result of the consistent interventions by the CBN. However, we expect the naira to trade within the region of N362/$ - N364/$ as manufactures begin to build inventories ahead of the festive period.



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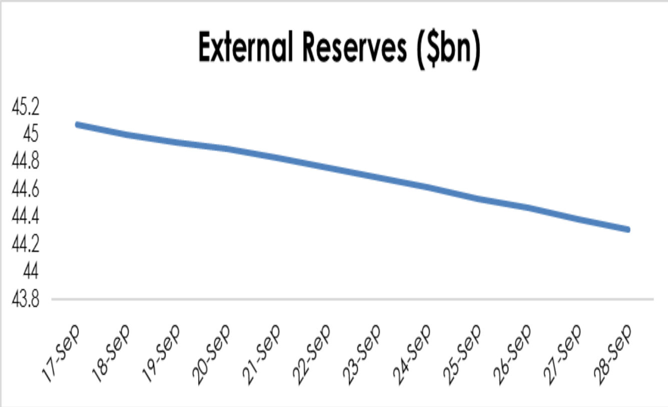
External Reserves

Nigeria's gross external reserves declined to close the period at $43.35bn on October 11th from $45.07bn on September 17th. This was primarily due to increased capital flight amid political tensions and increased demand for forex. The depletion of the external reserves resulted in an import cover of 10.79 months.

Outlook

Depletion of the external reserves is expected to persist in the near term, owing to the increased capital flight ahead of the 2019 elections and higher interest rates in the U.S.



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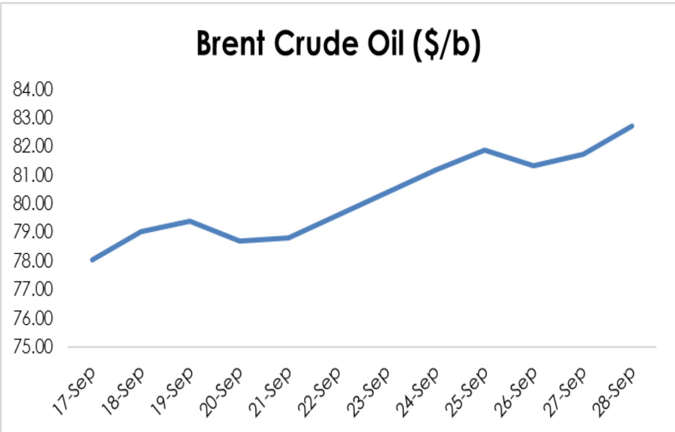
COMMODITIES MARKET - EXPORTS

Oil Prices

Oil prices rose steadily during the period from $78.05pb on September 17th to $82.72pb on September 28th. Average oil price for the period was $80.28pb, 7.37% higher than the average of $74.77pb for the corresponding period in August. The increase is largely due to the looming U.S sanctions on Iran for oil. It is worth stating that oil prices rallies to a 56-month high of $86pb on October 3rd, before retreating to close at $81pb on October 12th.



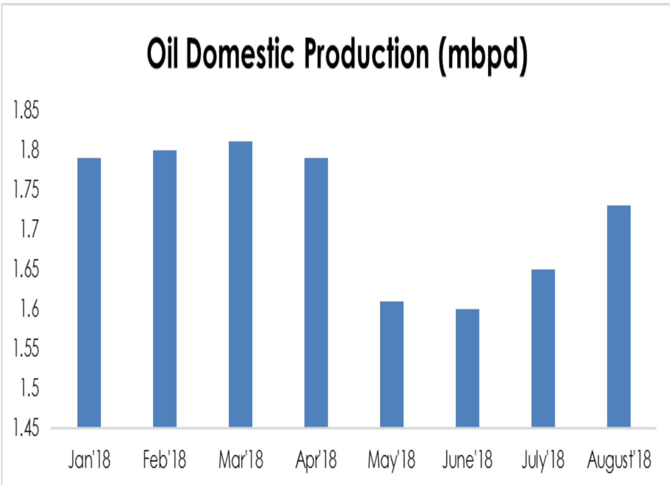
[22]

Outlook

We expect the bearish trend in oil prices to be sustained. The expected increase in output from Saudi Arabia and other oil producers are likely to offset lower Iran output estimated at 1mbpd. However, we expect prices to remain above $70pb.

Oil Production

Nigeria's domestic oil production increased by 1.74% to 1.75mbpd in September from 1.72mbpd in August. This was partly due to the re-opened Trans-Forcados and Nembe Creek trunk lines. However, Nigeria's oil rig remained flat at 14 in september.[23]



[24]

[21] CBN
[22] Bloomberg
[23] Bakers Hughes
[24] OPEC

Outlook

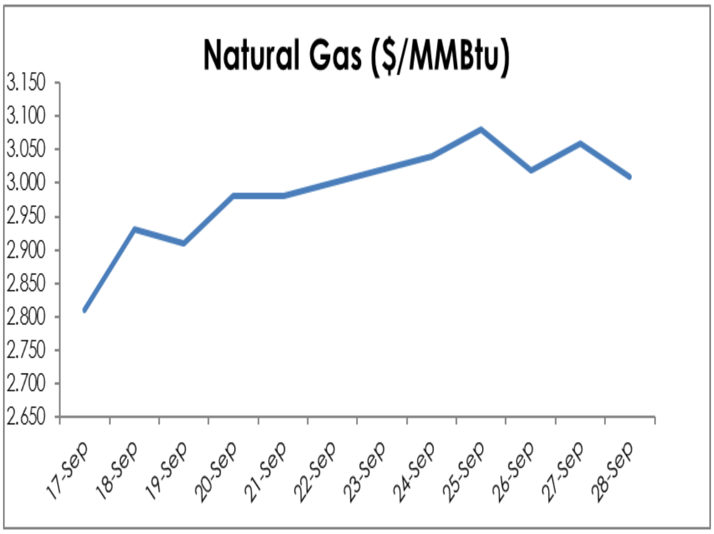
The increase in Nigeria's oil production is expected to be sustained in the near term following production activities at oil terminals.

Natural Gas

Natural gas prices rose by 7.12% from $2.81/mmbtu on September 17th to $3.01/mmbtu on September 28th. The price rise was majorly due to the strong demand in the U.S.

Outlook

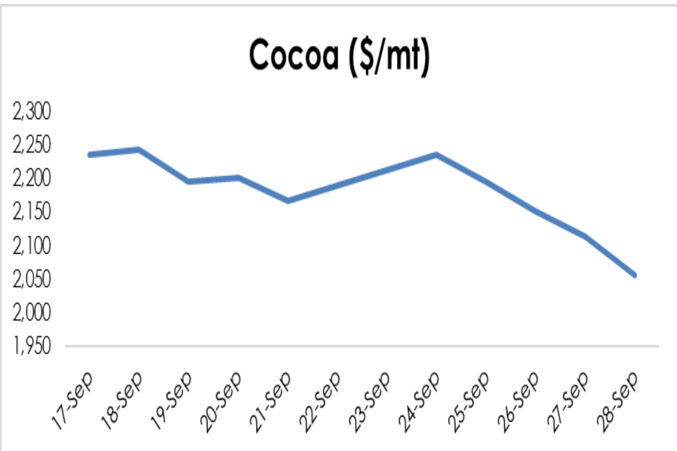
Demand for natural gas in the U.S is expected to rise in the near term as the winter season approaches. This would likely raise prices.



[25]

Cocoa

Cocoa prices recorded a choppy movement during the period. The price of the commodity declined by 8.01% to $2,057/MT on September 28th, from $2,236/MT on September 17th. This price decrease was largely driven by rising global production.



[26]

Outlook

We expect the downward trend of cocoa prices to persist in the coming weeks following reports of increased production in Ghana.

[25]Bloomberg.

[26]Bloomberg.

IMPORTS

Wheat

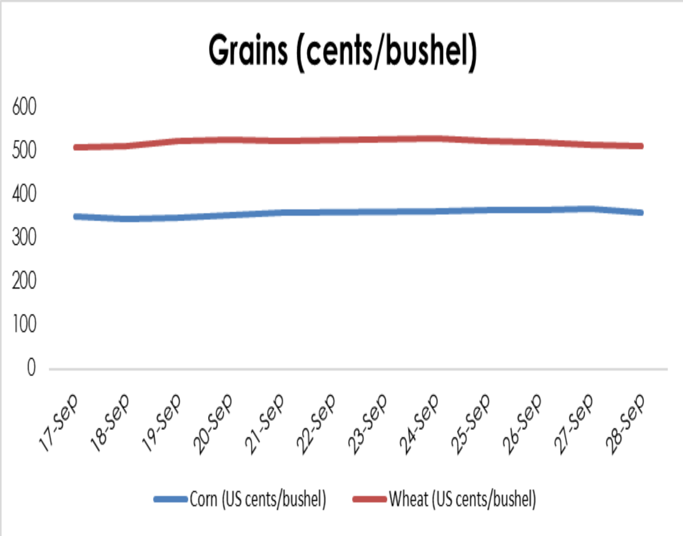
Wheat prices increased by 0.59% to $5.09/ bushel on September 28th, from $5.06/bushel on September 17th. The increase was mainly due to weak Russian exports during the period.

Corn

Corn prices rose by 2.30% to $3.56/bushel from $3.48/bushel. The price was supported by weak harvests in the U.S.

Grains- Outlook

Grain prices are expected to maintain their bullish trend in the near term. Reports of reducing Russian wheat exports and delayed corn harvests in the U.S due to rains would support this rise.



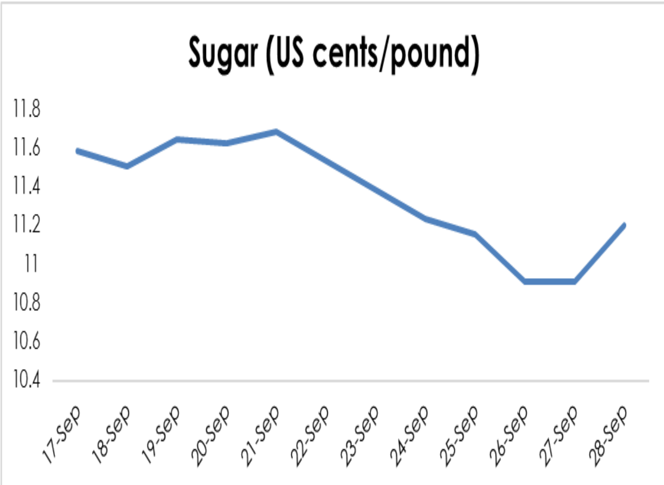
[27]

Sugar

Sugar prices fell by 3.28% to $0.1120/pound on September 28th, from $0.1158/pound, suppressed by increased sugar production in India.

Outlook

We expect the price of sugar to rise in the coming weeks following reports of unfavourable rains in India, which would affect sugar production.



[28]

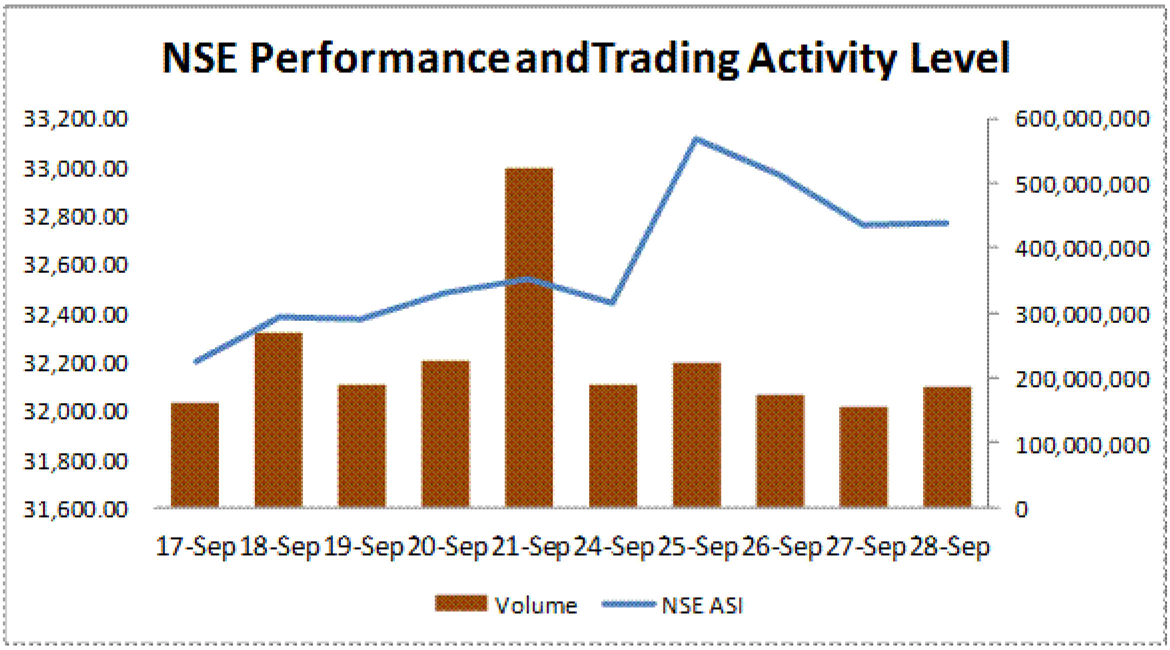
[27]Bloomberg.
[28]Bloomberg.

STOCK MARKET UPDATE

The NSE-All Share Index (NSE ASI) bucked its bearish streak in the second half of September, gaining 1.36% to close at 32,766.37 points on September 28 from the September 14th close of 32,327.59. The CBN Governor's statement that the issue with MTN would be resolved amicably calmed investor fears and partly drove a positive sentiment on the exchange. The NSE however remained in a correction territory. The market lost 14.32% YTD as at September 28.

The market rose in tandem with the ASI by 1.36% (N160bn) as the market capitalization closed the period at N11.96trn. The stock market traded at a price to earnings (P/E) ratio of 9.34x (September 28th), 0.65% increase compared to its close of 9.28x on 14th of September, 2018. During the review period, the NSE recorded 5 days of losses and 5 days of positive trading.

The market breadth was positive at 1.24x, as the number of gainers (47) outpaced the number of losers (38), while 84 stocks remained unchanged.



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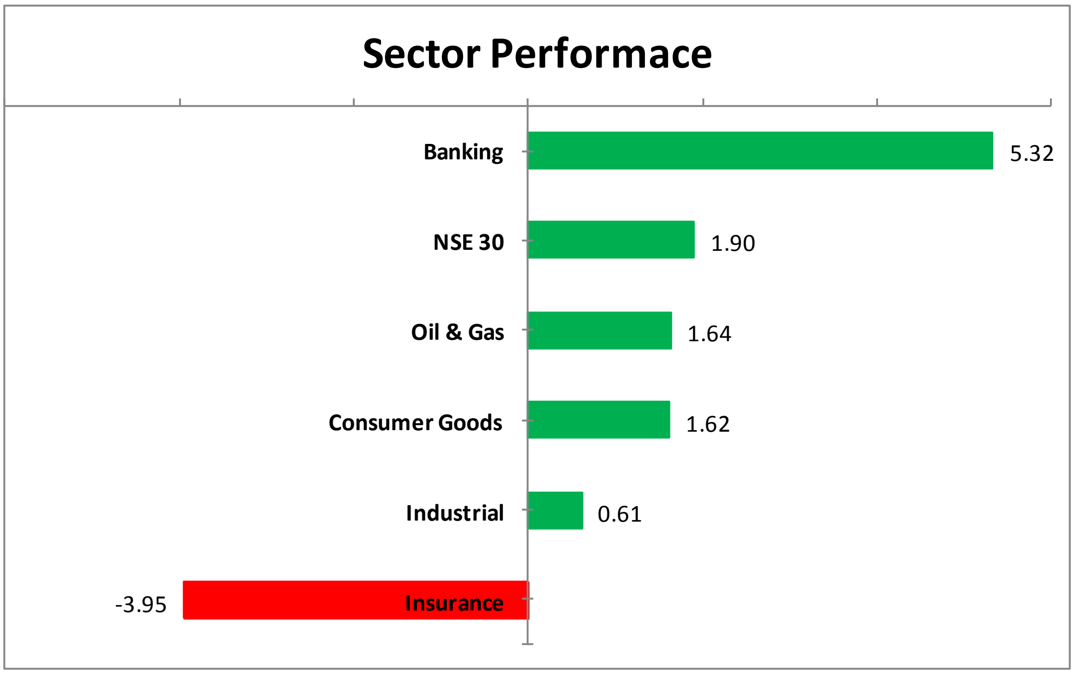
[29] NSE, FDC Think Tank

The bourse witnessed more trading activities in the second half of September. Average volume traded increased by 24% to 229mn units compared to 185mn units recorded in the first half of September. Average value of transactions showed the same trend as it was up 7.3% to N3.37bn in the review period.

SECTOR PERFORMANCE

In the period under review, the performance of the NSE sub-indices was broadly positive. The banking sector performed best, gaining 5.32%. Largely capitalized banking stocks such as United Bank for Africa Plc (14%), FBN Holdings Plc (9%) and Zenith Bank Plc (7%) drove this positive performance. Only the insurance sector lost (-3.95%).



[30]

The best performing stocks were FIRST ALUMINIUM NIGERIA PLC (37%), UACN PROPERTY DEVELOPMENT COMPANY LIMITED (24%), LINKAGE ASSURANCE PLC (19%), VERITAS KAPITAL ASSURANCE PLC (15%) and SKYE BANK PLC (15%).

TOP 5 GAINERS (N)				
Company	Sep'14	Sep'28	% Change	Absolute Change
FIRST ALUMINIUM NIGERIA PLC	0.30	0.41	37	0.11
UACN PROPERTY DEVELOPMENT CO. LIMITED	1.57	1.95	24	0.38
LINKAGE ASSURANCE PLC	0.59	0.70	19	0.11
VERITAS KAPITAL ASSURANCE PLC	0.26	0.30	15	0.04
SKYE BANK PLC	0.67	0.77	15	0.1

[30]NSE, FDC Think Tank

The least performing stocks were STANDARD ALLIANCE INSURANCE PLC (-20%), RED STAR EXPRESS PLC (-17%), CORNERSTONE INSURANCE COMPANY PLC (-17%), AXA MANSARD INSURANCE PLC (-15%) and CONSOLIDATED HALLMARK INSURANCE PLC (-9%).

TOP 5 LOSERS (N)				
Company	**Sep'14**	**Sep'28**	**% Change**	**Absolute Change**
STANDARD ALLIANCE INSURANCE PLC.	0.25	0.20	-20	-0.05
RED STAR EXPRESS PLC	5.45	4.50	-17	-0.95
CORNERSTONE INSURANCE COMPANY PLC.	0.24	0.20	-17	-0.04
AXA MANSARD INSURANCE PLC	2.30	1.95	-15	-0.35
CONSOLIDATED HALLMARK INSURANCE PLC	0.32	0.29	-9	-0.03

Outlook

Investors are expected to remain cautious of elevated political risks. The delayed impact of the US Fed's decision to raise interest rates could also reflect in more foreign portfolio investment exits from the bourse. These factors portend a reversal of the NSE's performance in the first half of October.

CORPORATE FOCUS : TRANSNATIONAL CORPORATION OF NIGERIA PLC

ANALYST'S NOTE

Power business delivers accelerated growth

Analyst Recommendation: Hold

Recommendation period: 365 days

Industry: Conglomerate

Market Capitalization: N51.22bn

Current Price: N1.27k

Target Price: N1.32k

Transnational Corporation of Nigeria Plc (Transcorp) recorded a 58% surge in revenue to N54.09 billion (bn) in the first half of 2018 (H1'18), from N34.17bn in H1'17. The impressive growth in top line revenue can be attributed to the 65.09% increase in inflow from the power generation segment.

Like revenue, Transcorp's cost of goods sold also increased, albeit at a slower pace. Costs increased by 52.94% to N29.52bn in H1'18. This can be largely attributed to the high cost of natural gas and fuel, a key input in power generation. Natural gas and fuel costs recorded a 63.05% spike, rising to N24.77bn in H1'18. The spike was partly due to increased usage, but largely due to the volatility in gas supply.

Agriculture and oil and gas portfolios continue dry spell

Although the group operates four business segments, only the power and the hospitality segments generated N54.09bn revenue in H1'18. The remaining two segments, the agro-allied and oil and gas divisions, recorded no income during the period. However, the management of Transcorp is looking to optimize its current portfolios. It will begin commercial operations in the oil and gas sector, converting its Oil Prospecting License (OPL) 281 to an Oil Mining Lease (OML), and it plans to dispose of the agro-allied subsidiary (Teragro).

Staff and consultancy expenses undermine operating efficiencies

Transcorp's performance in H1'18 surpassed the previous period, as management exercised discipline over most of its operating costs. This slowed the growth in its operating expenses to 34.99% (N7.23bn). However, the inability to tighten staffing expenses and professional fees weighed on the group's cost containment efforts.

Profitability buoyed by favorable financing options

Transcorp recorded a remarkable rise in profit after tax (PAT), despite a 190% increase in income tax expenses. PAT rose by 161% to N10.88bn in H1'18, compared to N4.16bn in H1'17. Despite the 58% boost in output (revenue), Transcorp's finance cost rose by only 7% to N5.01bn. This performance signals that the group's financial woes, particularly its abysmal performance in 2016, might be a thing of the past. However, the infrastructure gap, especially in the power sector, will continue to weigh on funding and associated costs.

Performance in tandem with market trend

The Nigerian Stock Exchange (NSE) All-Share Index (ASI) has been adversely affected by election uncertainties and higher real yields in advanced economies. This is evident from the bearish market trend, which has so far lost 16% in 2018. Like the NSE ASI, Transcorp stocks have lost 14% of their value in 2018. Consequently, we place a HOLD recommendation on Transcorp's stock, as its performance has been largely suppressed by weak investor sentiment.

INDUSTRY AND COMPANY OVERVIEW

Transcorp was incorporated in 2004 as a private limited liability company and subsequently quoted on the Nigerian stock exchange (NSE) in 2006. The group, through subsidiaries and affiliates, operates a diverse investment portfolio in the hospitality, power, agro-allied and oil and gas sectors.

Power business remains group's lifeline

The group generates all its revenue in Nigeria and its power generation portfolio is the major driver at 85%. It operates one of the six power generation plants in Nigeria, the Ughelli power plant located in Delta State. The plant has an installed generation capacity of about 1000 megawatts (MW), but only generated 160MW at the initial stage of the acquisition. Since the acquisition of the plant in 2013, Transcorp's management has increased its generation capacity by 324% to 678MW, owing to the boost from its gas turbine.

Despite the impressive returns from this business segment, the sector has been weighed down by a low return on investment, which has stifled the injection of additional investment. This is coupled with the delayed implementation of cost reflective tariffs, which are expected to improve the attractiveness of the sector.

The hospitality segment continued to consolidate on its leadership position. Transcorp's hotel chains maintained dominance in the segment despite the slowdown in economic growth. Upgrade projects, especially in Transcorp Hilton Abuja, are expected to boost the income generating capacity of the group.

Transcorp bites the bullet to minimize losses

Transcorp has shown great commitment to divest from its agro-allied business segment. This will be largely immaterial to the group's financial position, as the segment contributes a minute amount to revenue and accounts for less than 0.10% of assets. The performance of the agro-allied segment has been significantly below par over the last seven years.

Income Statement for Transcorp Plc				
N'000	**2014**	**2015**	**2016**	**2017**
Revenue	41,338,136	40,753,506	59,424,619	80,284,959
Cost of sales	(13,703,608)	(16,423,115)	(29,258,812)	(43,860,652)
Gross profit	27,634,528	24,330,391	30,165,807	36,424,307
Administrative expense	(12,281,087)	(9,613,617)	(10,377,108)	(11,751,949)
Other operating income	391,578	504,460	475,959	690,696
Other gains - net	(2,119,549)	(186,816)	451,361	668,943
Operating profit	13,625,470	15,034,418	20,716,019	26,031,997
Finance income	1,897,400	1,165,227	363,016	498,259
Finance expense	(7,791,272)	(6,818,984)	(8,303,471)	(9,670,480)
Foreign exchange gain/(loss)		(6,061,132)	(18,703,912)	(4,554,229)
Profit before tax	7,731,598	3,319,529	(5,928,348)	12,305,547
Income tax expense	(4,427,338)	(1,287,972)	4,801,350	(1,698,271)
Profit for the year	**3,304,260**	**2,031,557**	**(1,126,998)**	**10,607,276**

Balance Sheet for Transcorp Plc				
N'000	**2014**	**2015**	**2016**	**2017**
Property, plant & equipment	93,518,593	109,761,030	124,660,561	141,835,592
Intangible assets	38,451,180	38,886,750	38,951,969	39,517,340
Investment property	2,738,164	1,706,600	1,706,600	1,706,600
Debt and equity securities	-	1,764,937	2,207,943	4,971,353
Deferred tax	-	-	3,356,550	3,348,918
Prepaid lease rental (long term)	35,000	5,000	58,704	53,010
Non-current assets	134,742,937	152,124,317	170,942,327	191,432,813
Inventories	1,682,224	4,597,456	4,722,545	4,646,609
Trade and other receivables	27,938,086	31,353,769	54,104,539	83,827,859
Prepaid lease rental (short term)	30,000	30,000	30,000	16,741
Debt and equity securities	3,431,598	358,887	-	
Cash and cash equivalent	2,930,517	14,419,520	2,361,320	5,598,282
Current assets	36,012,425	50,759,632	61,218,404	94,089,491
Total assets	**170,755,362**	**202,883,949**	**232,160,731**	**285,522,304**
Ordinary share capital	19,360,499	19,360,499	20,323,996	20,323,996
Share premium	7,213,368	7,213,368	6,249,871	6,249,871
Treasury shares	(137,790)	(345,819)	(345,819)	-
Other reserves	-	(587,547)	(14,662)	2,777,781
Retained earnings	30,070,219	28,138,355	27,207,214	31,961,979
Equity attributable to equity holders	56,506,296	53,778,856	53,420,600	61,313,627
Non controlling interests	33,248,555	33,726,375	33,027,997	34,394,170
Total equity	89,754,851	87,505,231	86,448,597	95,707,797
Borrowing (long term)	37,138,699	61,844,507	72,943,568	75,589,945
Deposit for shares	-	2,410,000	2,410,000	2,410,000
Deferred tax	11,593,635	10,502,430	7,158,798	7,159,053
Non-current liabilities	48,732,334	74,756,937	82,512,366	85,158,998
Trade and other payables	13,769,258	17,687,690	31,586,476	64,846,974
Taxation	5,984,570	5,695,106	4,137,597	1,424,147
Borrowing (short term)	10,639,349	15,363,985	25,600,695	36,509,388
Advance deposit	1,875,000	1,875,000	1,875,000	1,875,000
Current liabilities	32,268,177	40,621,781	63,199,768	104,655,509
Total liabilities	81,000,511	115,378,718	145,712,134	189,814,507

The management of Transcorp has intensified efficiency efforts to maximize shareholder wealth and consolidate the subsidiaries' leadership positions in their respective sectors.

Tony Elumelu, CON, currently serves as the Chairman of Transcorp Group. Mr. Elumelu is renowned for his strategic focus on capacity development and talent management to achieve accelerated growth. This aggressive but consistent approach has been quintessential to the success of businesses under the stewardship of Mr. Elumelu. In addition, he has set the strategic direction of the group and has leveraged extensively on his network in the financial industry, as well as other complementary affiliates.

His commitment towards long-term growth is also evident from the management's introduction of Gas Turbines 15. This is expected to boost the national grid output and ultimately productivity of the power generation segment.

The management team of Transcorp is currently led by Adim Jibunoh, who oversees the strategic operations of all subsidiaries. As an ardent portfolio manager, he has ensured synergy between sister subsidiaries. To also improve the quality of decision making and uphold the seamless process of service delivery, he manages the provision of value-added services to subsidiaries. This initiative has aided the group's strides in cost containment and efficiency gains.

Managing Director

Adim Jibunoh

Chairman of the Board of Directors

Tony Elumelu

THE BULLS SAY

* Improved gas supply and generation capacity of the power plant
* Opportunity to consolidate position in the hospitality segment, leveraging the Hilton brand
* Diversified business portfolio
* Stability in the economic and business environment

THE BEARS SAY

* Policy risk – Transcorp could be adversely affected by federal government policy reversals, especially in the power segment
* Tariff hikes are unlikely in an electoral cycle
* Foreign exchange risk – Transcorp is highly reliant on internationally sourced infrastructure, especially in the power generation segment
* Electoral cycle risks – restraining business tourism and initiatives, reducing occupancy rates in the hospitality segment
* High infrastructure requirements and complex bureaucracy in an unpredictable business environment discourages investment
* The long payback period is a deterrent to investments in infrastructure
* Low dividend yield

RISK AND OUTLOOK

Policy and financial risk management are key areas of focus that will determine the success of Transcorp. The group is highly susceptible to the business cycle and remains exposed to government policies and regulations, given the group's investments in sectors with high government interest and intervention.

Its business relationship with the government also exposes the group to credit risk, as the government accounts for over 25% of trade receivables. This risk is mainly from its operations in the power sector. A threat to the income generating capacity of the government will adversely affect the cash flow position of Transcorp.

Transcorp also faces foreign exchange risk; due to the extensive investment in infrastructure and equipment which are settled in foreign denominated currencies. This exposes the group to fluctuations in the exchange rate. To mitigate this risk, the group holds a portion of its cash and cash equivalents in foreign currencies. As a result, Transcorp's treasury team monitors currency movement on an on-going basis.

In addition, the decision by the management of Transcorp to convert its OPL to an OML for commercial operations by the start of 2019 will expose the group to both exogenous and endogenous factors that affect typical oil exploration companies. Hence, factors such as oil bunkering, militant activities, crude oil prices and logistics will be key risk criteria for the management.

APPENDIX - OUR VALUATION

Using the Discounted Cash Flow (DCF) methodology, we estimated a stock price of N1.35, which is a 6.3% upside on the current price of N1.27 as at September 25, 2018. The discount rate (Weighted Average Cost of Capital (WACC)) of 14.1% was derived using a 14.39% risk free rate (FGN 5-year Bond as at August 2018), a Beta of 2.185, after a tax cost of debt of 6.4%, and a market risk premium of 6.34%. The long term cash flow growth rate to perpetuity calculated is 3.5%.

Based on our analysis above, we place a HOLD rating on the stock.

DCF Valuation			
N'000	**2018E**	**2019E**	**2020E**
EBIT	33,396,667	37,114,596	42,583,319
Less: Taxes	(10,019,000)	(11,134,379)	(12,774,996)
EBIAT	23,377,667	25,980,217	29,808,323
Plus: D&A Expense	4,255,068	3,736,742	4,124,797
Less: CAPEX	(11,889,142)	(12,034,731)	(19,485,010)
Less: Change in working capital	1,659,747	2,328,655	2,834,584
Free Cash Flow (FCF)	17,403,339	20,010,883	17,282,694
WACC	13.8%	13.8%	13.8%
Present Value (PV) of FCF	15,295,191	15,456,490	11,732,171
	2018	**2019**	**2020**
Terminal value			173,951,639
Present value of terminal value	118,085,196		
DCF Calculation	**Valuation**		
PV of explicit period	42,483,851		
PV of terminal value	118,085,196		
Enterprise Value	160,569,047		
+ Cash	5,045,289		
- Borrowings	(112,099,333)		
Equity Value	53,515,003		
Share price	**1.32**		

Important Notice