

# FDC Bi-Monthly Update

Volume 10, Issue 07

April 22, 2020



A Financial Derivatives Company Publication

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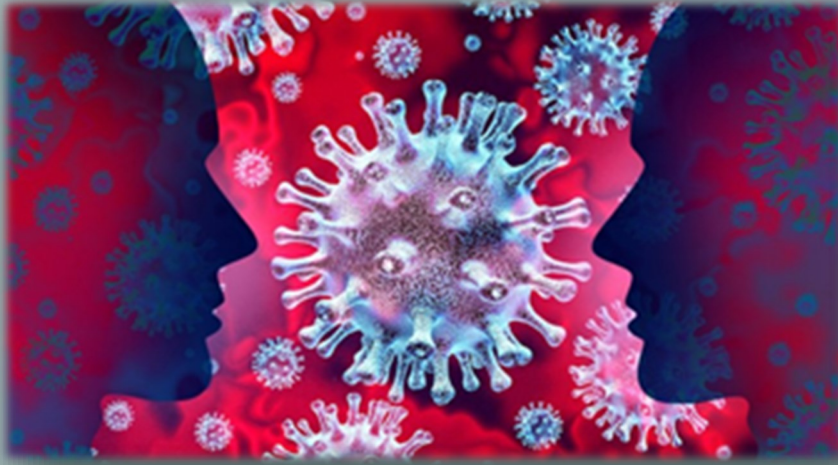
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*After corona there will be no wahala!*



My illiterate uncle in Ubeji, Warri South Local government, asked me on the phone yesterday, the difference between 419 and C-19 (covid-19). I hesitated before responding and said to him in Itsekiri dialect- why the question and what is the link? His response was as intriguing as the question. He said he was around during the influenza flu of the 1950s and he was fully briefed by our great grandfather about the 1918 flu. He said that whilst the devastation was probably more in the past, the noise this time and the coordinated lockdown are unprecedented. He said at age 95, he was not in the mood to be fooled by any Government, leader or relative. He said that illicit gin and roots are the antidote to this virus, flus and most ailments. He therefore said to me “send me a carton of Bols Schnapps or Chelsea gin with some lemon” and he can assure me that he will be around even after the postponed Olympic Games next year.

He quickly referred me to the NCDC update, which showed Bayelsa state with no infections or fatalities. I told him “uncle, it is because they are not testing, that is why”. He said, “shut up silly boy, it is because our neighbours are deep into gin consumption and not any silly testing” and I said, “Uncle, that was Putin and the Russians thought before the coronavirus wreaked havoc on them

He said in Itsekiri, “Please forget that matter, not everything is economics and science”. He said that before Abraham, I was, silly boy”

The import of this conversation is that whilst the covid-19 discussion is raging, the communication is becoming boring and confusing. The mixed signals on social distancing and the lockdown are eating into public motivation and the credibility of the messengers. Therefore, messaging and consistency needs to be well coordinated and streamlined.

### *Post covid-19 World*

People in general and Nigerians in particular are getting bored and frustrated with the news media and the obsession with covid-19 from the radio to the TV and print media; it is as if there was no world before Coronavirus. Any death is ascribed to covid-19. People were dying before Corona and will die after the virus.

This note is to look at the economy and businesses in a post Covid-19 world. After the Great Depression, Franklin D. Roosevelt embarked on major public works and spending programmes termed as the “New Deal”. Based on Keynesian countercyclical spending thinking that in times of depression, government spending can help economies in depression recover faster than private investment. It was based on the 3R’s - relief, recovery and reform. The outcome was the reform of Wall Street, relief for farmers and unemployed and social security for all. Many economists question John Maynard Keynes that all of this spending i.e. printing money in the short run was going to lead to hyperinflation and imbalances in the long run. Keynes’ popular response was that “in the long run we are all dead”.

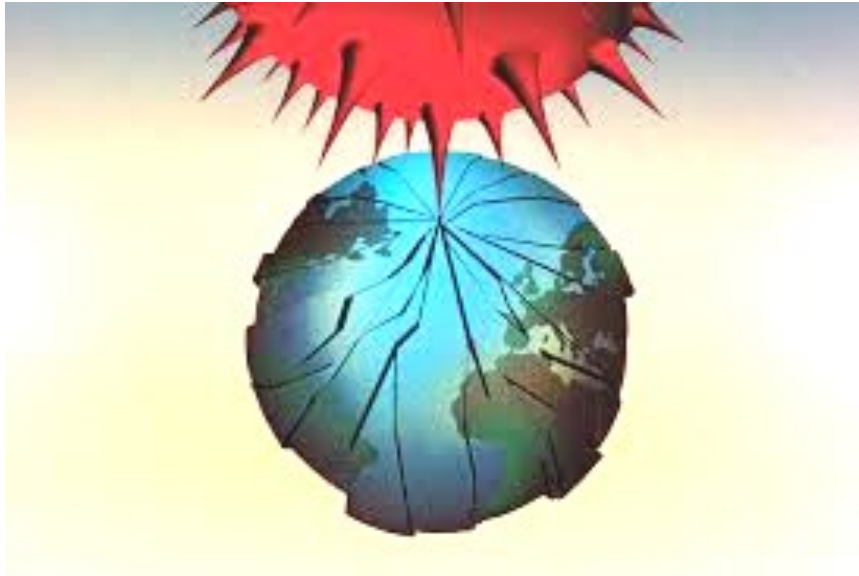
### *The economy will be in recovery in August 2021*

So after all this grammar and economics jargon, what is the bottom line and where will you be in August 2021? Covid in the name of Jesus will be over and the economy will be on slow recovery mode, growing at +1.05% after reaching a low of -4.5%. Inflation rate would have flattened out and dropped to 8-9% and the naira will be trading at rates close to its real effective exchange rate (REER) at the time. There is no point guessing if the price of bonny light will be back up to \$38-40pb and production will be back to 1.3-1.4mbpd. Pump price of petrol will be back at N150-160 per litre after adjusting for exchange rate fluctuations.

## *Consolidation and survival before prosperity*

These are the starting points with consolidation in most sectors and rapid recovery in construction, trading and mostly telecommunications. The Nigerian stock market will rally again to a market capitalization of over N15trn and IPOs from MTN etc. The payment service banks will have Nigeria's equivalent of MPESA in Kenya and guess what, banking consolidation will be on the front burner again. Not just that, the Nigerian government will sell down some its stake in the oil joint ventures, which will now be incorporated. But wait a minute, the Dangote refinery will be christened one of the largest in the world and the refining hub of Western and Central Africa. So it is not just bad news, after corona there will be no wahala.

# The disruptive impact of Covid-19



Covid-19 has brought the global economy to its knees. The lockdowns, social distancing and self-isolating rules in various countries have resulted in a virtual economic paralysis and what could likely be the worst financial crisis since the Great Depression.

## *Covid-19 & the Nigerian economy*

Nigeria is not spared from the economic implications of the Coronavirus pandemic. Transmission channels of Covid-19 on the economy include the oil price effect, global financial conditions, external trade effect and the foreign investment flows. This explains why agencies such as the IMF and EIU are projecting a contraction in Nigeria's GDP growth to -3.4% and -2.2% respectively. Whilst both agencies estimate a slight recovery in 2021 to 2.4% and 0.9%, this will depend largely on the adoption of key policy reforms.

## *Impact on sectors*

There is no doubt that Coronavirus has disrupted activities in virtually all sectors ranging from aviation, sports, hospitality, education amongst others. The only sectors benefiting during the pandemic are sectors offering essential services which include Pharmaceuticals, health care and telecommunications amongst others.

Table 1: Winners in a stormy market	
<b>Attractive sectors</b>	<ul style="list-style-type: none"> <li>• ICT</li> <li>• Health care</li> <li>• Pharmaceuticals</li> </ul>
<b>Resilient sectors</b>	<ul style="list-style-type: none"> <li>• Consumer goods</li> <li>• Banking</li> </ul>
<b>Moderate impact</b>	<ul style="list-style-type: none"> <li>• Agriculture</li> <li>• Food &amp; Beverage</li> </ul>

## Government response

In order to mitigate the fallout, the fiscal and monetary teams have introduced stimulus packages of varying magnitudes:

**Monetary team:** Contrary to market expectations and the examples of advanced central banks, Nigeria's monetary team is yet to cut its benchmark interest rate. This could be due to the complexity of lowering interest rates at a time of heightened inflationary pressures. Countries such as the US, UK, South Korea, Japan and China that have cut interest rates since the Covid-19 outbreak all boast of single digit inflation rates compared to Nigeria's double digit inflation rate of 12.2%.

**Fiscal team:** The initial response of the fiscal team was to revise the 2020 budget assumptions including the total estimated spending as well as the oil price (\$30pb) and production benchmark (1.7mbpd). With the current free fall in Brent price and the additional OPEC output cuts of 9.7mbpd, these assumptions may need to be revised again in the near term. In addition, the Ministry of Finance has sought for financial support of \$6.9bn from multilateral agencies including IMF, World Bank and the AfDB. In reality, Nigeria stands a greater chance of securing these loans with the adoption of a market determined and efficient price model for exchange rates and refined petroleum products.

Is this enough?

The question on the minds of Nigerian business owners and consumers remains – is this enough? Analysts are of the opinion that the FGN stimulus which represents a miserly 0.34% of GDP is not sufficient to move the needle. A simple guideline policy makers can use with regards to the necessary palliatives include the following:

**Appropriateness;** is this the necessary move at this time? Is this solution tailor made for Nigeria? Have all possible options been exhausted?

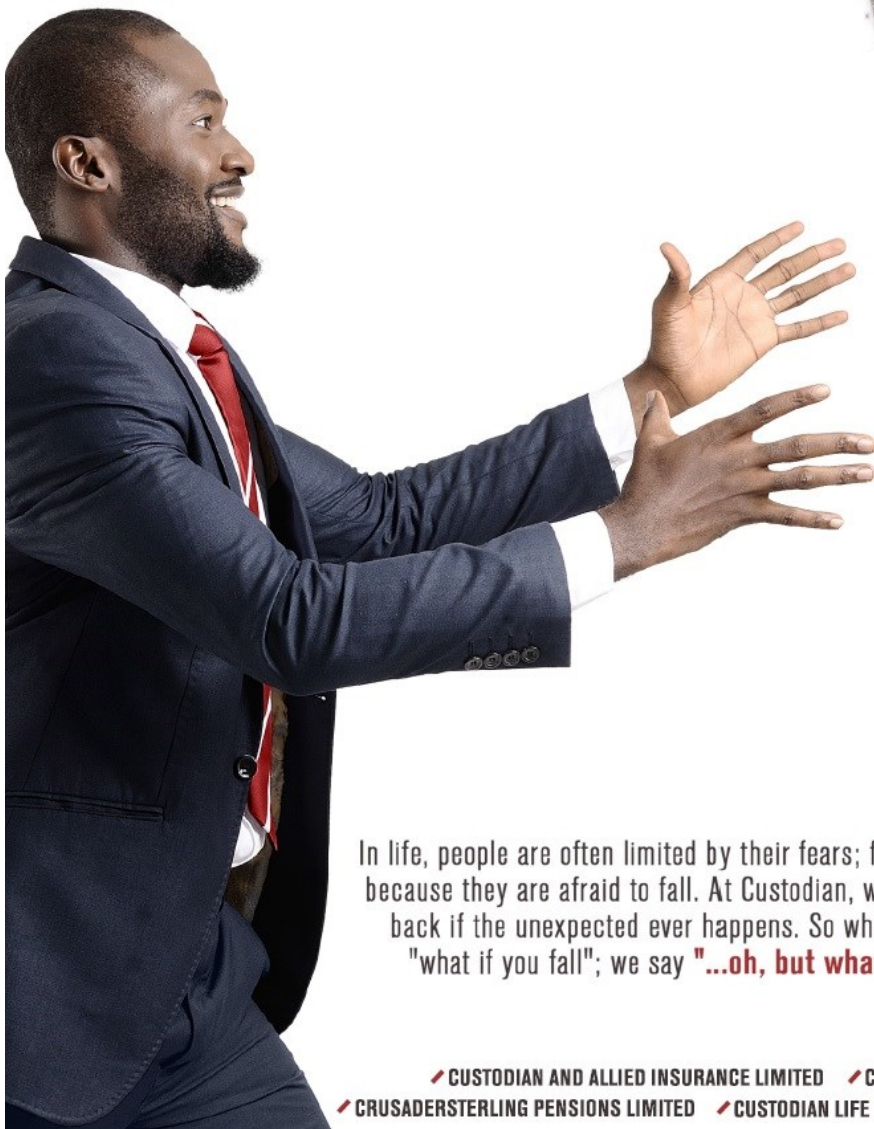
**Auspiciousness:** Will Nigerians be better off? How to ensure the palliatives get to the appropriate people?

**Adequacy?** Is this the right dose? Is this evenly distributed across affected states?



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# *Softness of the Oil Market today & impact on Nigeria*

Since the historic output cut by OPEC and its allies, oil prices have continued to trade below \$30pb, contrary to market expectations. West Texas Intermediate (WTI) traded in negative territory (-\$37pb) for the first time ever due to the slump in oil demand and storage constraints. This is an indication of the softness of the global oil market and the fact that the global oil market is more demand sensitive than supply. With the largest oil consumer (China) likely to post a meager growth rate of 1% in 2020, oil prices at current levels of \$27pb and possibly lower may be the order of the day. Other demand factors that have suppressed the price of oil include the suspension of all flights except for essential services and the postponement of summer trips and tourist events.



## *What does this mean for Nigeria?*

Part of the Federal Government's policy responses to the contraction in economic activities and drop in fiscal revenue was the adjustment of the 2020 budget oil price benchmark to \$30pb from \$57pb initially approved. The oil production benchmark was adjusted from 2.18mbpd to 1.7mbpd, with a further decline to 1.4mbpd being considered. All revenue projections initially made have become null and void and the fiscal deficit of N1.85trn earlier projected is looking more like N4.9trn. The bad news is that the Nigerian economy was already in a dire state prior to the slump in oil prices and the COVID -19 pandemic. The country was already facing challenges such as sub-optimal growth, fiscal and external imbalances and negative total factor productivity.

## *Impact of oil price plunge in Nigeria*

**Fiscal Balance-** The average price of oil YTD is \$47.43pb. This is 58.18% above the FGN's budget benchmark of \$30pb. This coupled with a 35.78% reduction in oil production (from 2.18mbpd to 1.4mbpd) will impact significantly on Nigeria's fiscal position. The government has requested for \$6.9bn from multilateral organizations to boost its funding needs, which are now focused on addressing the impact of the COVID-19 pandemic on the economy. State governments depend partly on oil receipts to meet their debt obligations. We are anticipating a further decline in FAAC disbursement in subsequent months. However the new exchange rate of N360/\$ used to convert oil revenues may cap the losses as evident in April's disbursement, which increased by 9.1% to N634.72bn. This means that states will struggle to pay salaries and meet other obligations.

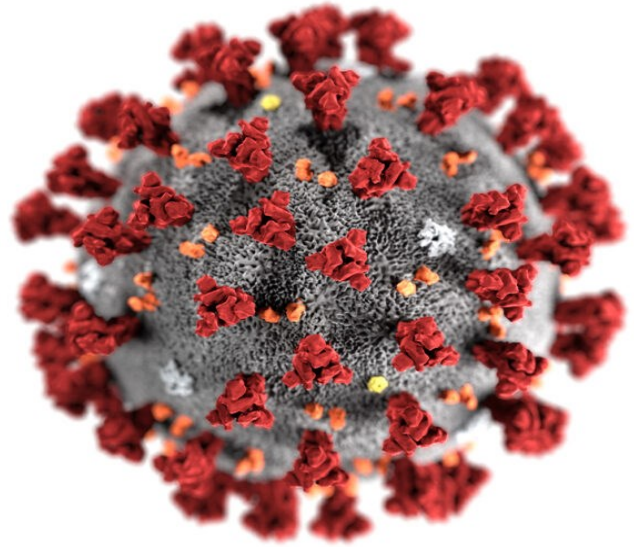
## *External balance*

**External reserves-** Nigeria's external reserves level has depleted 12.33% (\$4.76bn) so far this year to its current level of \$33.84bn (April 16, 2020). Over 70% of Nigeria's forex receipts are from oil proceeds. While on the demand side, forex demand pressures have been muted due to suspension of flights and shutdown of schools, the supply of dollars has dropped sharply and may continue to fall as oil revenue slides. The IMF is projecting an average oil price of \$35pb in 2020.

**Exchange rate:** The CBN in March adjusted the official exchange rate and IEFX rate to N360/\$ and N380/\$ to reflect current market realities. At the parallel market, the naira is trading within a range of N415/\$ and N430/\$ (that is even if it is available to buy). Due to the high dependence on oil proceeds, the softness of the oil market may lead to a deterioration of the terms of trade, thereby heightening the pressure on the currency. This may call for further adjustments to the currency if need be.

# Covid-19: Probability of Fatalities

Covid-19 continues to ravage both developed and developing economies, heightening the risk of an economic recession. In the last five months, the number of global confirmed cases skyrocketed to over 2million with death cases rising to approximately 140,000. The US, Spain, Italy, Germany and France were the most hit countries while Libya, Benin, Gambia, Mauritania and Botswana were mildly affected. For Nigeria in particular, the total number of confirmed cases increased to over 400 with fatal cases crossing the single digit band.



The rapid spread of the virus has forced countries to deduce a correlation between the fatalities and socio-economic indicators such as life expectancy and median age as well as climatic conditions such as temperature. For instance, Italy with a life expectancy of 83.6 years, median age of 45.5 years and temperature of 13.45oC was one of the most hit economies while Benin with a life expectancy of 61.5

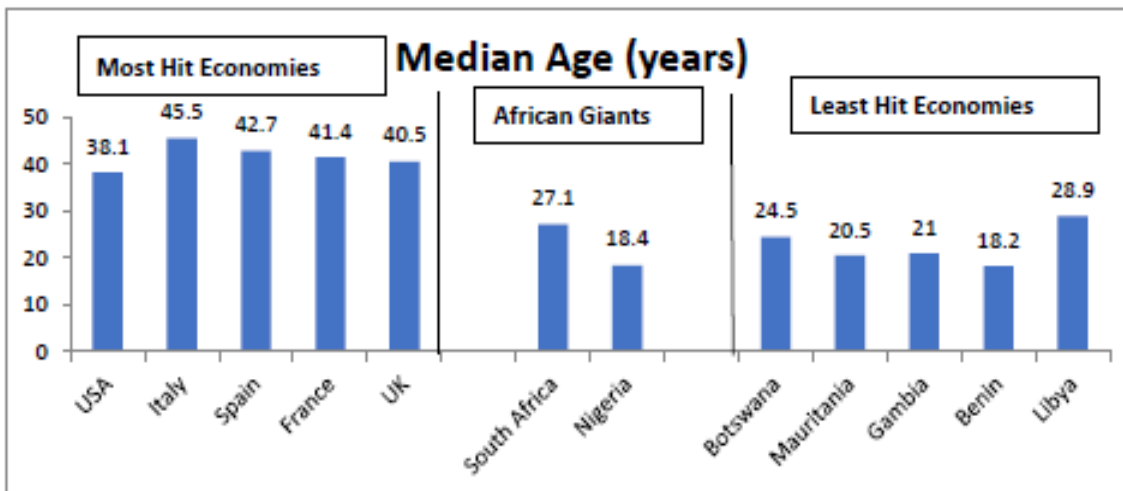
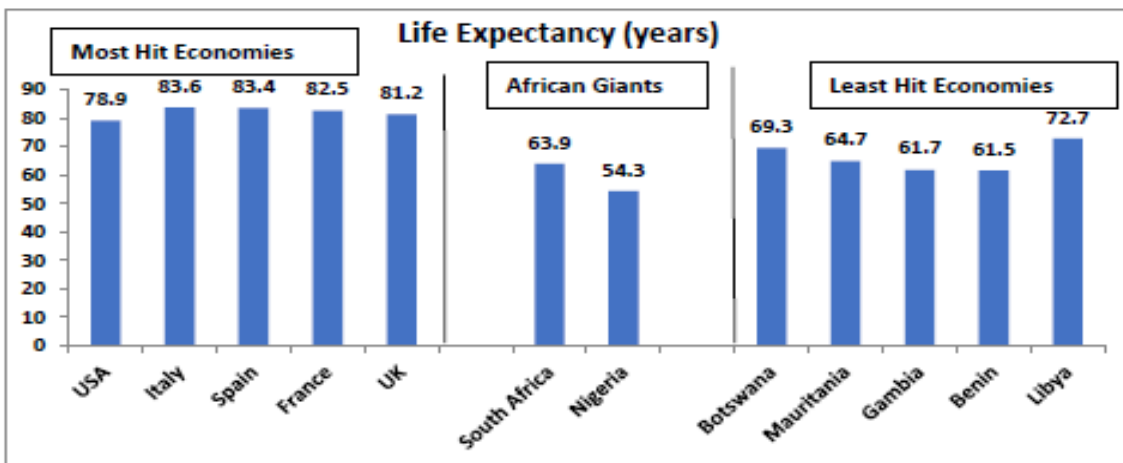
years, median age of 18.2 years and temperature of 27.55oC was among the least affected countries.

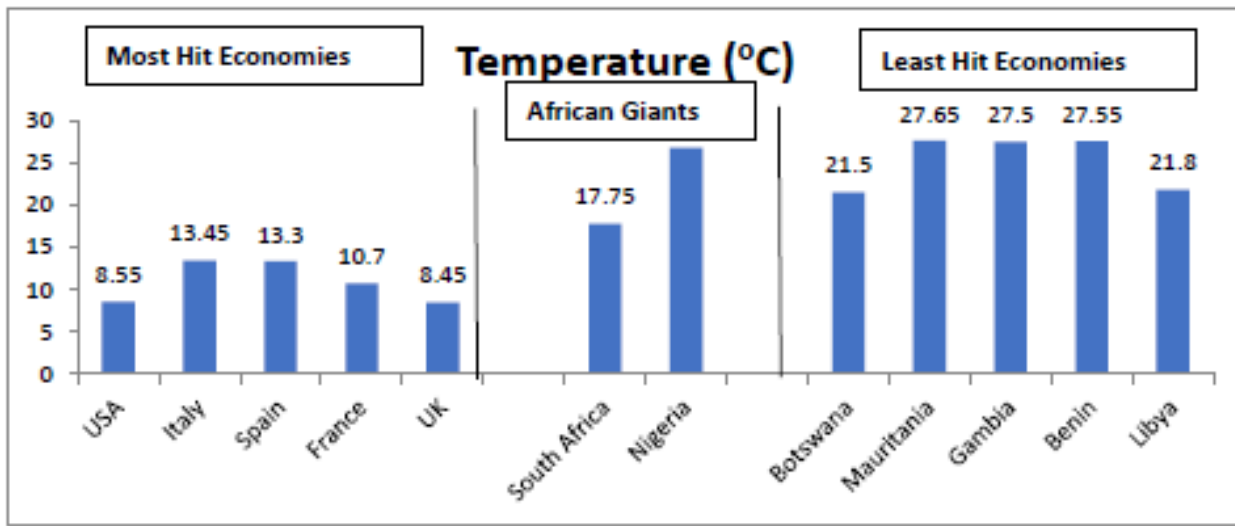
It is in this light we sought to establish the correlation between fatal cases and the socio-economic indicators and climate conditions of 20 countries. The observations consist of the 10 most hit economies and the 10 least economies.

	Correlation coefficient
Life expectancy & Fatalities	0.68
Median Age & Fatalities	0.67
Temperature & Fatalities	-0.60

From the table above, there seems to be a strong positive correlation between life expectancy and fatalities as well median age and fatalities. This suggests that countries with high life expectancy and median age tend to be vulnerable to Covid-19 death. This is likely because these countries have a high aged population with low immune system and possible pre-existing health conditions. Also, there seems to be a negative correlation between temperature and fatalities. By implication, countries with hot and humid weather tend to be less vulnerable to Covid-19 death.

**Appendix – Source: UNDP, CIA World Factbook**



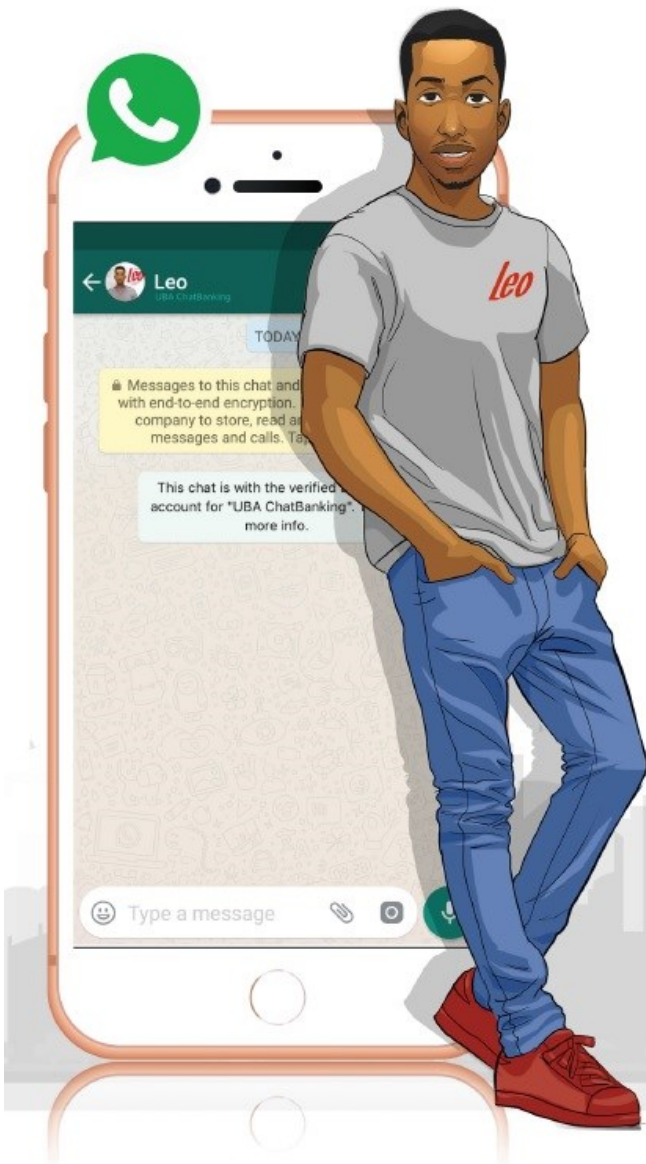




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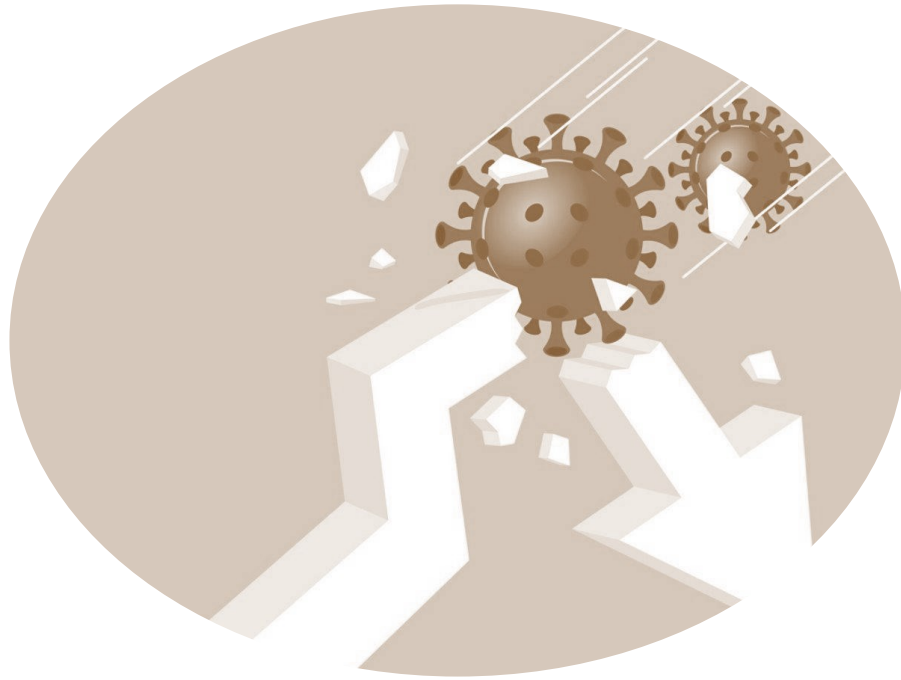
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# Nigeria's Impending Recession



The International Monetary Fund (IMF) estimates that the coronavirus pandemic will cause a global recession in 2020 that could be worse than the one triggered by the global financial crisis of 2008-2009. However, it expects a recovery by 2021. The pandemic has sparked a global economic meltdown. The negative effect on growth comes through both demand and supply channels. As entire countries go into lockdown and economic activity grinds to a halt, negative consumer and business sentiment will impact demand negatively. At the same time, businesses have shutdown and the resultant disruption to global supply chains is still yet to be fully quantified.

*For Nigeria, it's no longer a case of if but when*

A second recession in four years is clearly on the cards. In 2016, it was the incomplete and belated response to the oil price crash that was the trigger. In 2020, the trigger is COVID-19 and pre-emptive measures on the part of the monetary and fiscal authorities will more than likely not be enough to stave off the looming threat. Four years ago, external reserves were \$25.84bn while external debt was \$11.26bn (mid-size buffers: \$14.58bn). Today, the buffers are down to \$9bn as external debt has more than doubled to \$26.94bn while reserves, though higher at \$35.94bn, have been in steady decline for about 10 months.



The impact of COVID-19 on the Nigerian economy has been 3-dimensional. The first is from the medical and health care perspective. The second is through a slowdown in trade, investment and project finance, considering that Nigeria's largest and most important trading partners are China and India – who are on lockdown. The third is through the plunge in oil prices and its devastating impact on macroeconomic stability.

### *A case of Déjà vu*

Nigeria's vulnerability to oil market turbulence is once again brought under the spotlight. The impact of an over 50% drop in oil prices since the start of the year will lower export revenues considerably from an estimate of \$65.7bn to \$40bn. Imports are now also projected to fall to \$43bn as both consumption and production slow. This means that the trade balance will fall to -\$3bn from \$11.4bn in 2019. According to the IMF a 10% drop in the price of oil in one year will reduce GDP growth by 1.3%. Therefore, if the current price of oil (\$28pb) persists through 2020, Nigeria's GDP will contract by 0.2%, guaranteeing a return to a recession.

The drop in oil prices means lower government revenue, which translates into many states having difficulty meeting salary and pension obligations. Capital projects will be suspended and contractors owed. This is negative for aggregate demand. When Q4'19 GDP growth numbers are broken down, it reveals that oil sector growth of 6.36% is the major driver of growth in the period. Of the 46 activities tracked by the NBS only 12 outperformed the national GDP growth rate of 2.55%. The 12 activities had an average of 6.85%. The other 34 activities had a combined average growth of -1.04%. The fast growing sectors including aviation are also highly vulnerable to the impact of the COVID-19.

As if the oil price shock is not bad enough, the rapid spread of coronavirus means entire industries are faced with shutdowns as a way of slowing down the outbreak. This is already resulting in job losses and Nigeria's unemployment figures could rise to 35-40%.

## Policy Fall Out

Nigeria's current expenditure plan (N10.59trn) is too small to meaningfully support the economy. The sharp drop in oil prices has necessitated a proposed cut of N1.5trn (\$5bn) to the 2020 budget and the adoption of a lower oil price benchmark of \$30pb. It also nudged the CBN into action after which it announced 6 policy responses:

- Extension of moratorium on loans
- Reduction of interest rates from 9% to 5%
- Creation of a N50bn (130mn euro) fund to support the economy
- Credit support for the healthcare sector
- Regulatory forbearance & strengthening of the loan-to-deposit rate policy

Fiscal and monetary coordination is needed now more than ever before. An exchange rate adjustment to N380/\$ means more revenue for the government as oil exports are priced in dollars but it also means higher import prices, including for food. To many, the CBN could not have chosen a better time to devalue the naira. Nonetheless, a similarly pressing issue would be when it would be a perfect time to remove petrol subsidies completely – certainly in a period of low oil prices. A lower pump price of Premium Motor Spirit (N123.50/liter) has been implemented and this will boost aggregate consumption, but not significantly.

The CBN has left interest rates unchanged as it weighs inflationary fears against the need to lower interest rates and stimulate growth. There is no telling how long this recession will last but sustainable and accelerated post-COVID-19 recovery will require economic restructuring that incentivizes long-term investment. Hopefully, the movement towards equilibrium factor pricing (exchange rate and petrol prices) will be a catalyst.

# *Africa's debt crisis hampers its fight against covid-19*



*Global Perspective: Culled from The Economist*

Governments must choose between paying creditors or saving lives

Economic crisis and covid-19 are forcing hard choices on most of the world. But the dilemma facing indebted poor countries is particularly acute. They can either pay foreign creditors or allow more of their citizens to die, say experts.

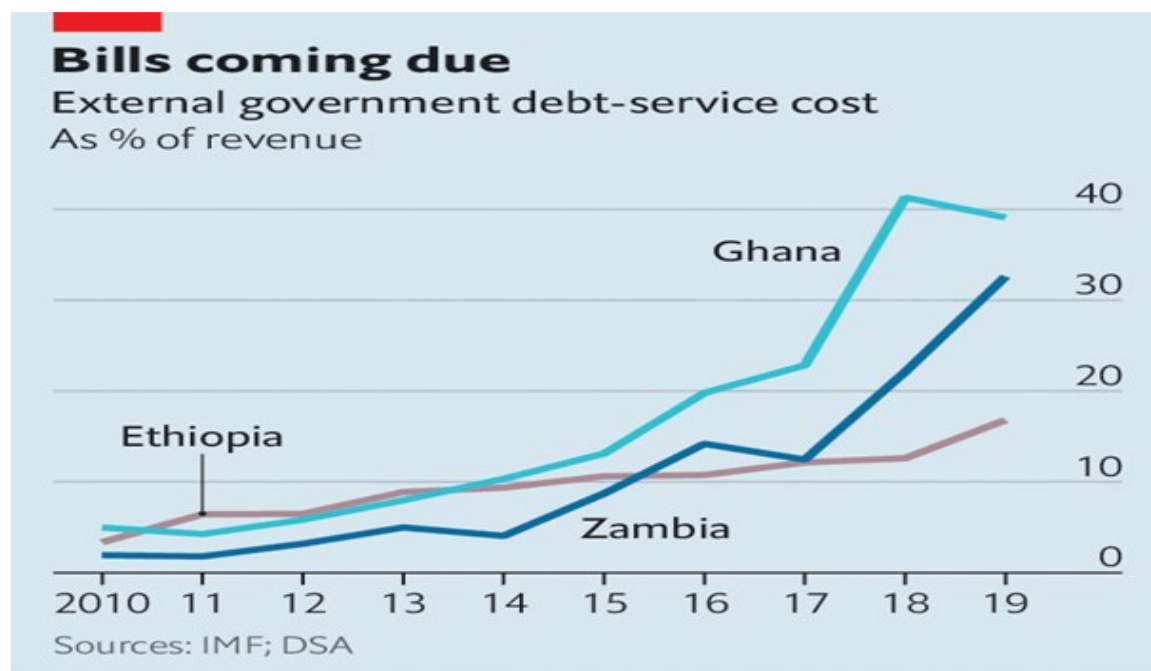
This dilemma is not new. In 2016 Angola spent nearly six times as much servicing its external debt as it did on public health care. Fifteen countries in sub-Saharan Africa spent more money paying creditors abroad than they did on doctors and clinics at home. But now, faced with a slump in revenues and skyrocketing borrowing costs as investors seek relative safety, many African governments are struggling to find the money to fight the pandemic and shore up their economies. Whereas rich countries are borrowing to spend about 8% of GDP on stimulus measures, African ones are spending just 0.8% of GDP.

This is because the virus has thrown petrol onto a slow-burning debt crisis. The countries most at risk of default—and, by definition, the least able to borrow affordably—are those with limited domestic savings and large external debts, such as Angola, Ethiopia, Ghana and Zambia. But they are not the only ones in trouble. Since 2010 average public debt in sub-Saharan Africa has risen faster than in any other developing region, from 40% to 59% of gdp in 2018. Most African countries have borrowed more than is prudent, said the IMF last year; 18 were classed as being in debt distress, or at high risk of it.

Many homeowners in Western countries are getting a mortgage holiday because of the pandemic. Might governments in Africa get the equivalent? The previous big round of debt relief for the continent came via the Heavily Indebted Poor Countries Initiative, which reduced foreign public debt of recipient countries from about 100% of gdp in 2005 to 40% by 2012. At the time Western governments and multilateral organizations, such as the IMF and World Bank, were the big-

lenders to Africa. Now, though, China is the continent's biggest bilateral creditor. Having signed loans worth more than \$146bn to African governments since 2000, it may not be as forgiving.

Africa's debt burden does more than divert spending from health care and stimulus to loan payments. It also discourages rich countries from helping out. Europe and America, in particular, worry that any aid they provide to African countries would eventually end up in the pockets of Chinese lenders.



The Economist

The World Bank and IMF have asked bilateral lenders to suspend debt payments from the world's 76 poorest countries. That would be a start, but would cover only a quarter of sub-Saharan Africa's total debt-service costs. Nevertheless, the appeal seems to have fallen on deaf ears in China, where officials say they will deal with African debt on a case-by-case basis. Analysts think China is loth to give up the political leverage that comes with being owed so much money. But, like other creditors, it may have to choose between orderly debt relief or chaotic defaults.

Even if China and other government lenders agreed to a pause on payments, states in sub-Saharan Africa might still use emergency funds to pay private creditors. The states owe bond investors \$115bn. (Commodity traders and domestic investors are owed, too.) Few commercial bonds are due for repayment before 2022, but interest must still be paid. If it is not, bondholders could demand full repayment. African finance ministers, hoping to protect their countries' creditworthiness, want donors to help pay the interest while negotiations take place

More than 100 international NGOs have called for a cancellation of all debt payments in 2020. But multilateral banks are reluctant to risk their own credit ratings and private bondholders are hard to corral. Lee Buchheit, a law professor at the University of Edinburgh, suggests changing American and British codes to stop lawsuits by angry bondholders against countries hit hard by covid-19.

Even if lenders listen to the NGOs and suspend all debt payments this year, there is still trouble ahead for African countries. Most collect relatively little tax. Low commodity prices have led to decreased revenues. And the countries that borrow the most also tend to be irresponsible spenders. Once this crisis is over, a wall of payments awaits them.

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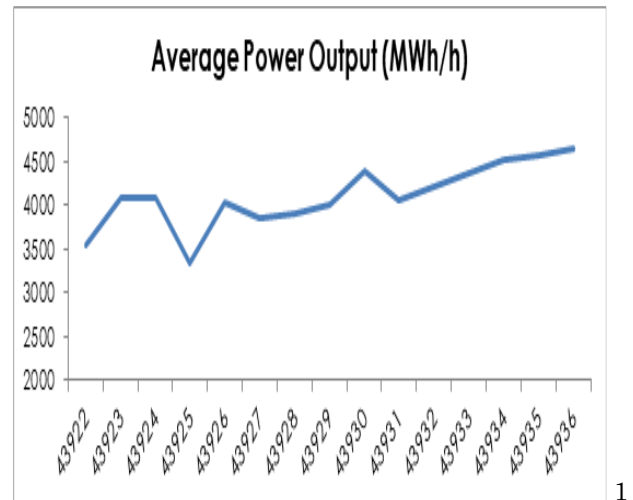
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# Macroeconomic Indicators

April 1st – 15th

## Power Sector

Average power output sent from the national grid stood at 4,104MWh/h, 8.57% higher than the average of 3,780MWh/h in the first half of March. During the period, the proposed electricity tariff hike to take effect on April 1 was postponed to July 1 due to the covid-19 virus that has disrupted economic activities. Gas remained the major constraint to power generation. Total constraint stood at 4,762MWh/h resulting in a revenue loss of N34.29billion (annualized at N411.48billion) in the sector.



## Outlook

As the rainy season commences, we expect an uptick in hydropower generation and this would support electricity supply in the coming months.

## Impact

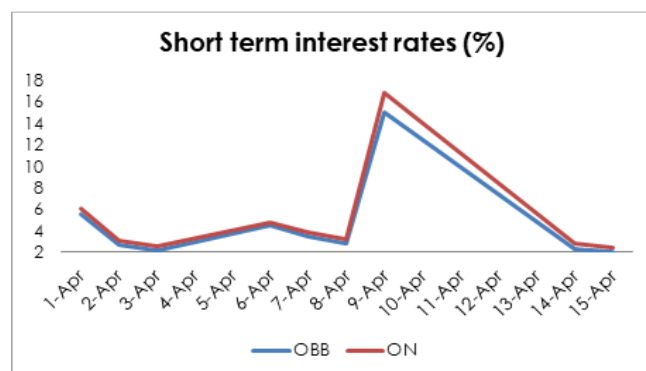
An increase in power supply will lower the operating cost of individuals working remotely due to the lockdown.

## Money Market

The average opening position rose by 100.36% to N530.86bn from N264.95bn in the corresponding period of March. This was mainly due to lower CBN forex intervention. OMO maturities (N395.28bn) were higher than OMO sales (N43.45bn), resulting to a net inflow of N351.83bn. On April 9, there was OMO auction N39.35bn, only the 341-sday tenor was offered at 12.80%pa.

On the average, the short-term interbank rates (OBB, O/N) fell by 856bps to 4.79%p.a from 13.35%%pa in the corresponding period. OBB and ON rates closed the period at 2.00% p.a and 2.42%pa respectively.

On April 15, there was a total primary market auction of N58.49bn, which was oversubscribed by 130.89%. Meanwhile, yields declined across all tenors at both the primary and secondary markets.



On April 15, there was a total primary market auction of N58.49bn, which was oversubscribed by 130.89%. Meanwhile, yields declined across all tenors at both the primary and secondary markets.

### Primary market

T/bills Tenor	Rate on April 01 (% pa)	Rate on April 15 (% pa)	Direction
91	2.20	1.93	↓
182	3.30	2.74	↓
364	4.30	4.00	↓

### Secondary Market

T/bills Tenor	Rate on April 01 (% pa)	Rate on April 15 (% pa)	Direction
91	2.20	2.16	↓
182	3.82	2.90	↓
364	4.50	3.92	↓

### Outlook

We expect interbank rates to remain at current levels pending any significant inflows into the money market.

### Impact

Lower interest rates will support private credit growth. However, with the ongoing skeletal activities due to the lockdown, private borrowing will be tepid in the meantime.

### Forex Market

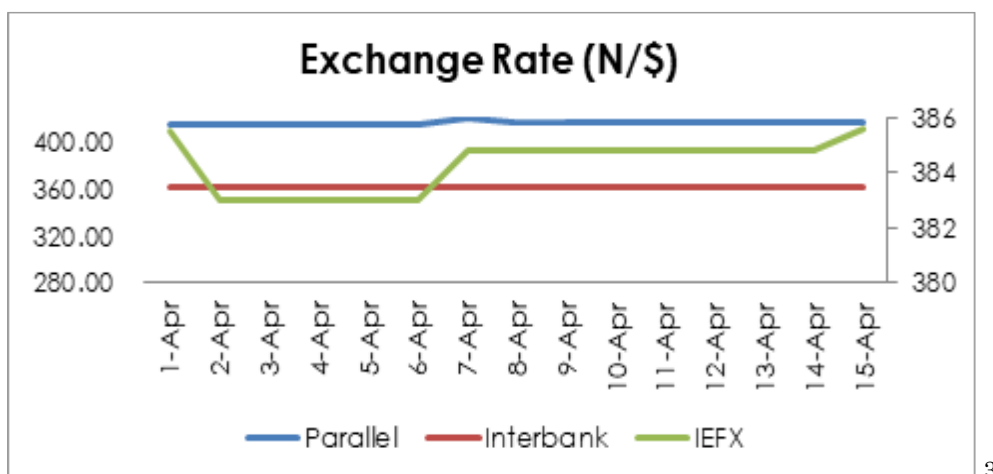
The Nigerian forex market is segmented with multiple exchange rates. The most important rate being the Investors and Exporters window (IEFX). No less than 55%-60% of Nigerian forex transactions are traded at this window. The CBN and most exporters and investors use this window. It serves as not only a source of price discovery but also a barometer for measuring potential and actual CBN intervention in the market. Some of the exchange rate determinants are balance of payments, capital inflows and trade balance.



## Exchange Rate

Currency pressures persisted in the forex market due to scarcity of dollars and speculative activities. In response, the CBN adjusted the currency at the IEFX window to N380/\$ and the official rate to N360/\$. On April 7, the naira depreciated to N420/\$ before strengthening marginally to close at N417/\$ in the parallel market.

Meanwhile at the IEFX window, the currency depreciated by 5.52% to close the period at N385.63/\$. In the midst of the lockdown and crawling cases of the virus in the country, commercial banks have reduced the naira card limits and the apex bank has encouraged more online transactions to maintain social distancing and curb the spread of the virus. In addition, the Bankers' Committee have agreed to provide financial support to the financially vulnerable in the country.



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## Outlook

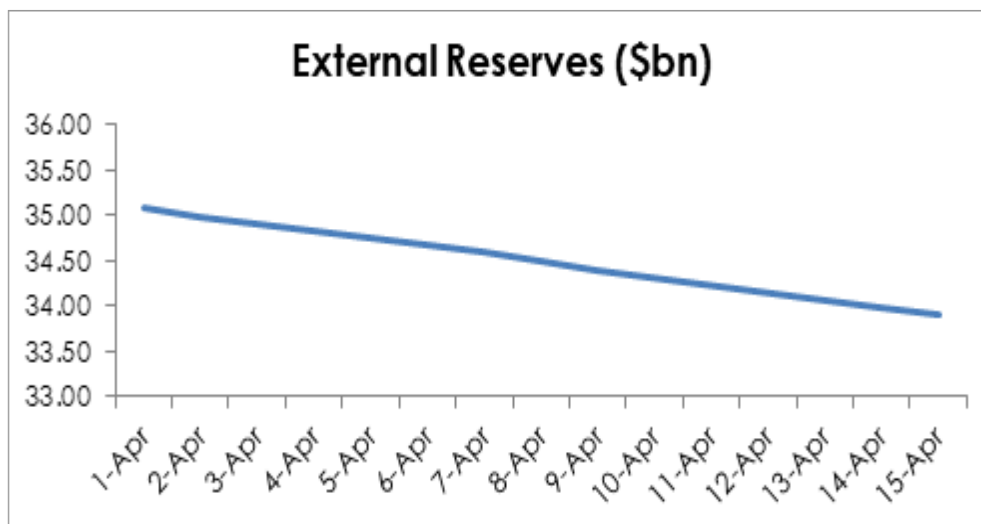
We expect currency pressures to persist in subsequent weeks as a result of the current market fundamentals.

## Impact

Nigeria is import-dependent and a weak currency will lead to an increase in imported inflation. Increases in prices coupled with the outbreak of the covid-19 pandemic in the country, could increase the risks in international trade and cause a further lull in investor confidence.

## External Reserves

Nigeria's gross external reserves recorded a 10-year low (\$33.91bn) on April 15. Reserves declined by 6.29% from \$36.26bn at the beginning of March. This is highly due to the plunging oil receipts and pressures in the forex market. Nigeria's import cover currently stands at 8.44 months compared to 9.03 months on March 2.



4

## Outlook

With the crash in oil prices (\$27.69pb), external reserves is expected to deplete further to \$32bn by next month.

## Impact

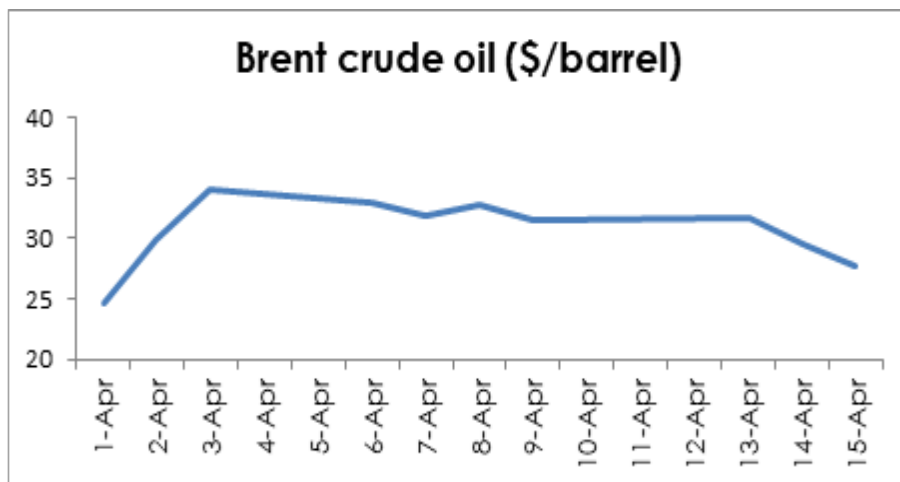
A decline in the government's buffers would reduce the capacity of the CBN to intervene in the forex market. It could also taper the ability of the economy to withstand both domestic and external shocks.

# Commodities Market - Exports

Nigeria is an export dependent economy. It derives over 80%-90% of its export revenue from crude petroleum and LNG.

## Oil Prices

Brent price slumped to \$27.69pb despite the historic output cut of 9.7mbpd set to take effect from May1. This is because the markets are skeptical about the likelihood of the cut to balance the existing demand/supply gap in the oil markets. Although, it was a significant recovery from \$24.74pb recorded on April 1, prices are still down 46.65% compared to the \$51.90pb on March 2. The weak global demand that is estimated to have fallen to 30mbpd so far in the year is exacting immense pressure on oil prices. The IEA also projects oil demand to decline further by 9.3mbpd.



5

## Outlook

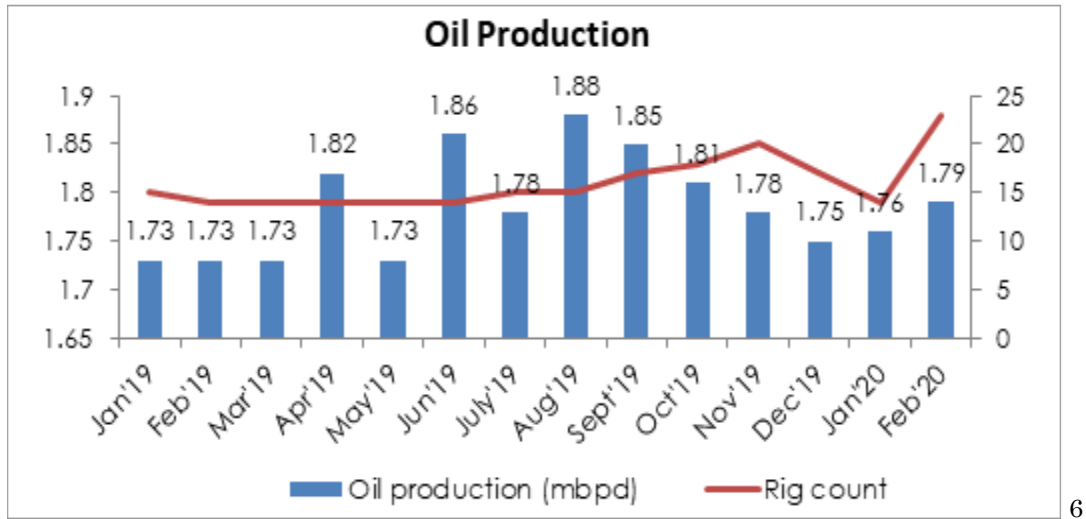
We expect a slow recovery in oil prices in the near term. Brent price is likely to trade between \$25pb - \$30pb.

## Oil Production

Nigeria's crude oil production spiked by 1.71% to 1.79mbpd in February from 1.76mbpd in January. This is also 1.13% above Nigeria's OPEC quota of 1.77mbpd. Conversely, the country's rig count declined from 23 to 21 in March. Oil output increased in Iraq, Nigeria, Angola, Congo and

<sup>5</sup>Bloomberg, FDC Think Tank

UAE, while it fell in Libya and Saudi Arabia. Disruptions in the oil market amid the covid-19 pandemic was a major burning issue at the OPEC+ meeting that happened in the month. Saudi and Russia quit their price feud to lead a global coalition of a 10% cut in global oil supply. Oil storage has also become a rising concern as oil producers are running out of storage facilities for their crude.



6

### Outlook

The cut in oil output by OPEC might not be sufficient to offset the impact of the declining global demand on the oil markets in the coming term.

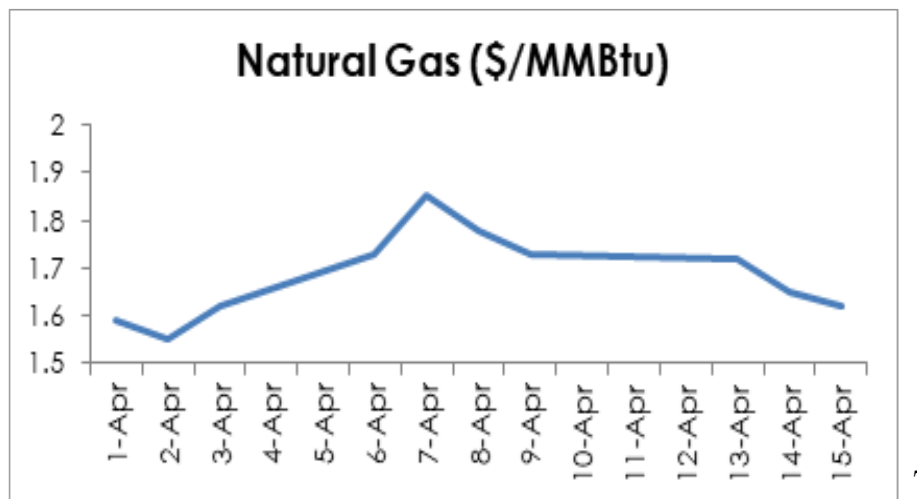
### Impact

Nigeria is a follower in the OPEC cartel structure and a decline in oil output could invariably mean a cut in the country's production quota to 1.47mbpd from 1.7mbpd. A fall in output will weigh negatively on Nigeria's fiscal revenues.

### Natural Gas

The price of LNG plunged sharply by 7.69% to an average of \$1.68/mmbtu from an average of \$1.82/mmbtu in the corresponding period in March. On April 7, natural gas prices recorded a 3-week high of \$1.85/mmbtu amid sentiments surrounding the cut in oil production and slight oil price recovery. The decrease was primarily due to the coronavirus that has tapered global demand for gas, especially from Europe.

<sup>6</sup>OPEC, FDC Think Tank



7

### Outlook

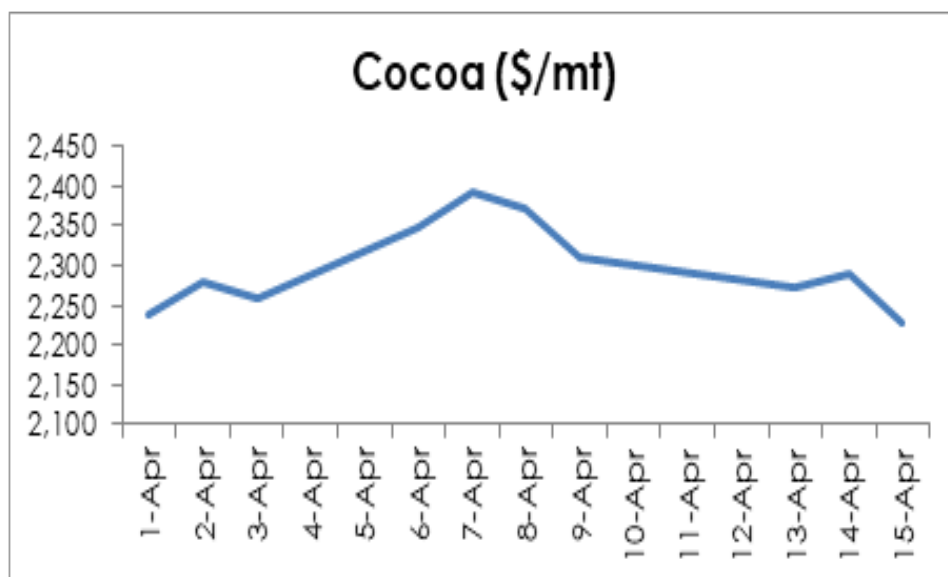
We expect an uptick in LNG prices as a cooler weather approaches in the US.

### Impact

Natural gas is a top export commodity for Nigeria, accounting for approximately 14.2%<sup>8</sup> of export revenue. A rise in the global price of LNG aided by increased demand will boost the country's LNG export earnings.

### Cocoa

The average price of cocoa fell by 9.98% to \$2,299/mt during the review period from an average of \$2,554/mt in the first half of March. Prices declined despite the unfavorable weather conditions in Ivory Coast that affected global supply. The slight pickup in cocoa prices was triggered by short-covering in cocoa futures as a result of weak US dollars.



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<sup>7</sup>Bloomberg, FDC Think Tank

<sup>8</sup>EIU

<sup>9</sup>Bloomberg, FDC Think Tank

## Outlook

Tightened supply from West Africa is expected to support cocoa futures in the coming months.

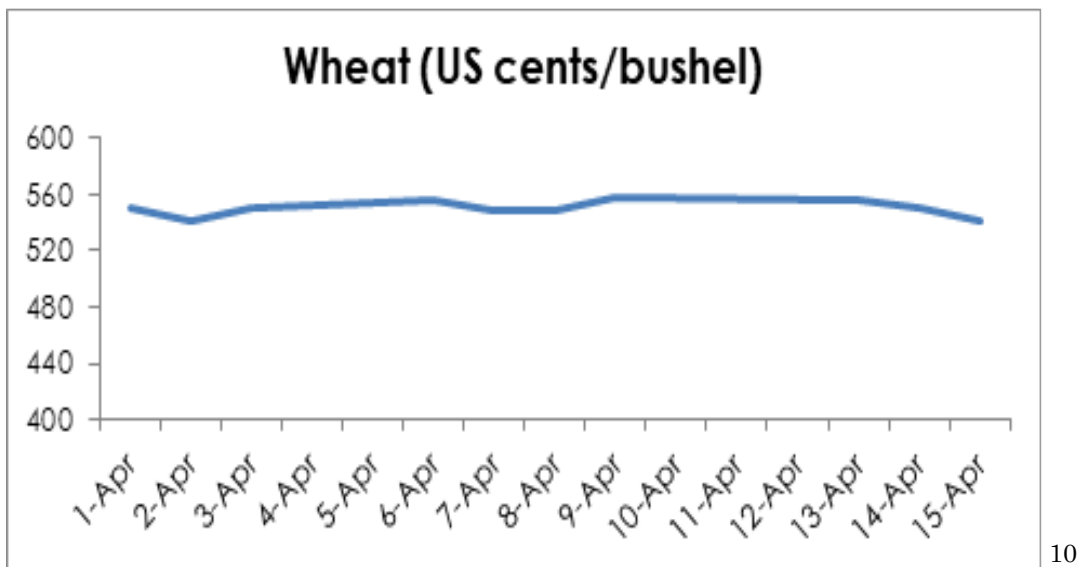
## Impact

An increase in global cocoa prices will bolster Nigeria's export revenue. However, if there is a moderate to severe spread of the virus in the country, cocoa production could decline significantly in the near term.

# Imports

## Wheat

On the average, wheat prices rose by 6.70% to \$549.63/bushel during the review period from \$515.14/bushel in the corresponding period in March. The uptick in prices is attributable to increased consumer demand amid stockpiling and panic buying of staples.

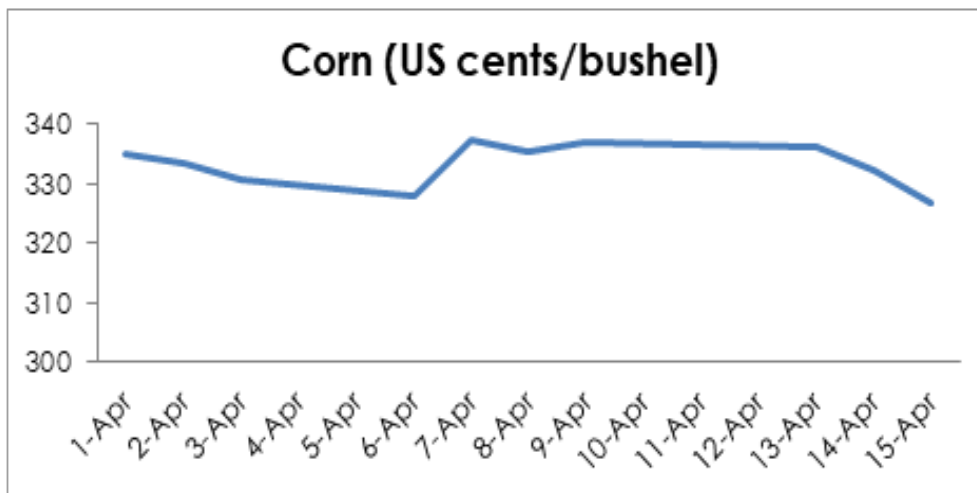


10

## Corn

Corn prices averaged \$333.15/bushel during the review period, 10.85% lower than the average of \$373.68/bushel recorded in the corresponding period in March. The bearish trend is highly due to the covid-19 pandemic that resulted in waning global demand, especially from ethanol producers.

<sup>10</sup>Bloomberg, FDC Think Tank



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### Outlook—Grains

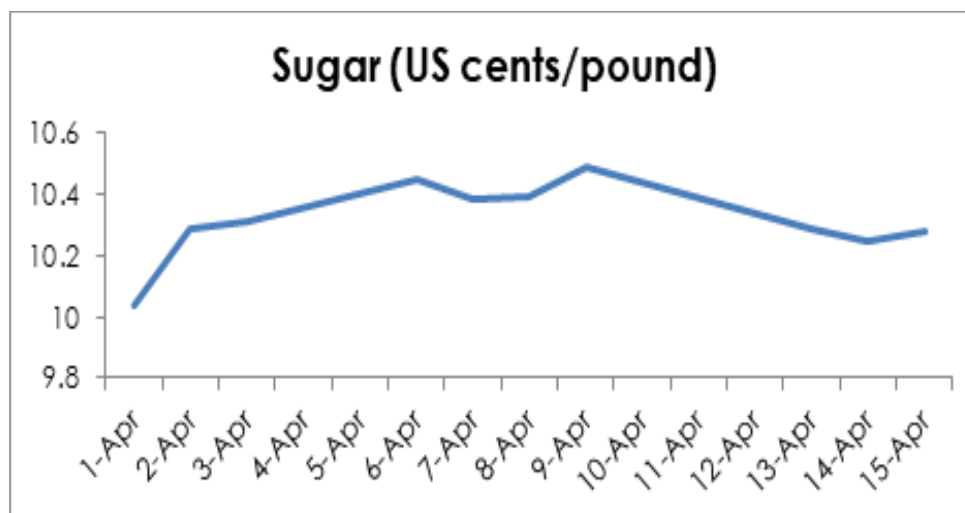
Stockpiling by consumers in a bid to stock up basic staples could keep grain price high in the near term. In addition, the commencement of the planting season is expected to support prices.

### Impact

An increase in the price of grains will increase the import bill of the country. It will also increase the cost of production of firms who depend on grains for their output like cereals and flour.

### Sugar

Sugar prices lost 18.56% to \$10.32/pound in the review period compared to the average of \$12.67/pound in the corresponding period in March. In addition, sugar prices reversed the declining trend on April 9 (\$10.49/pound) on the slight oil price recovery and sugar crisis in Pakistan. However, as Brazil announced its sugar output projections prices began to decline again.



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<sup>11</sup>Bloomberg, FDC Think Tank

<sup>12</sup>Bloomberg, FDC Think Tank

## Outlook

If Brazil increases production of sugar, supply will increase in the global market. Hence, we expect prices to taper in the near term.

## Impact

Declining global prices for sugar will lead to a fall in the country's import bill and a favorable balance of trade.



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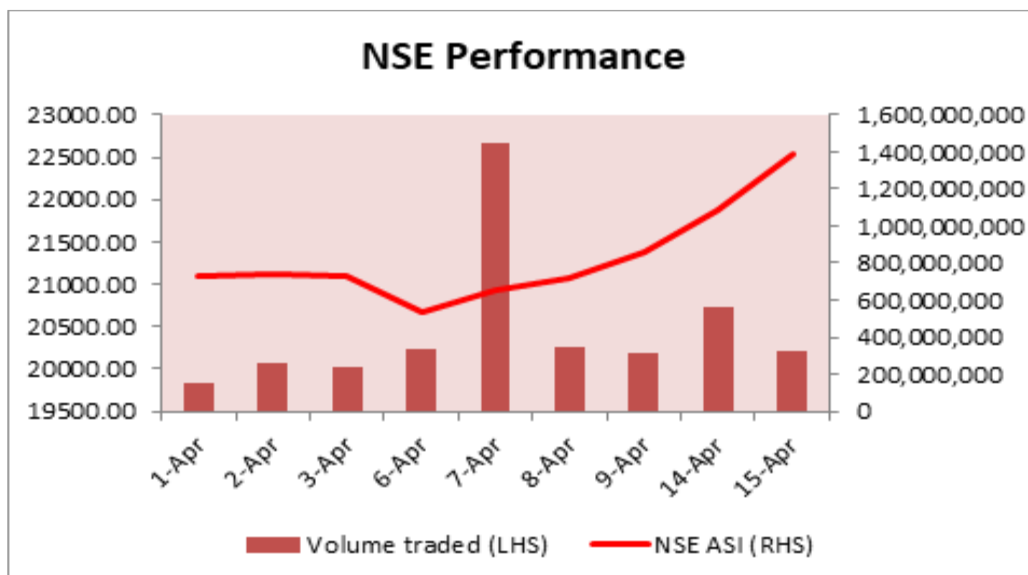
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# Stock Market Review

The

NSE ASI gained 5.82% to close at 22,539.94 points on April 15th relative to its close of 21,300.47 points on March 31st. This was due to a positive turnaround in investor sentiment and bargain hunting activities on the bourse. In the same vein, market capitalization rose by 5.86% (N65bn) to N11.75trn. In the 9-trading day period, the market gained in six days and lost in three.

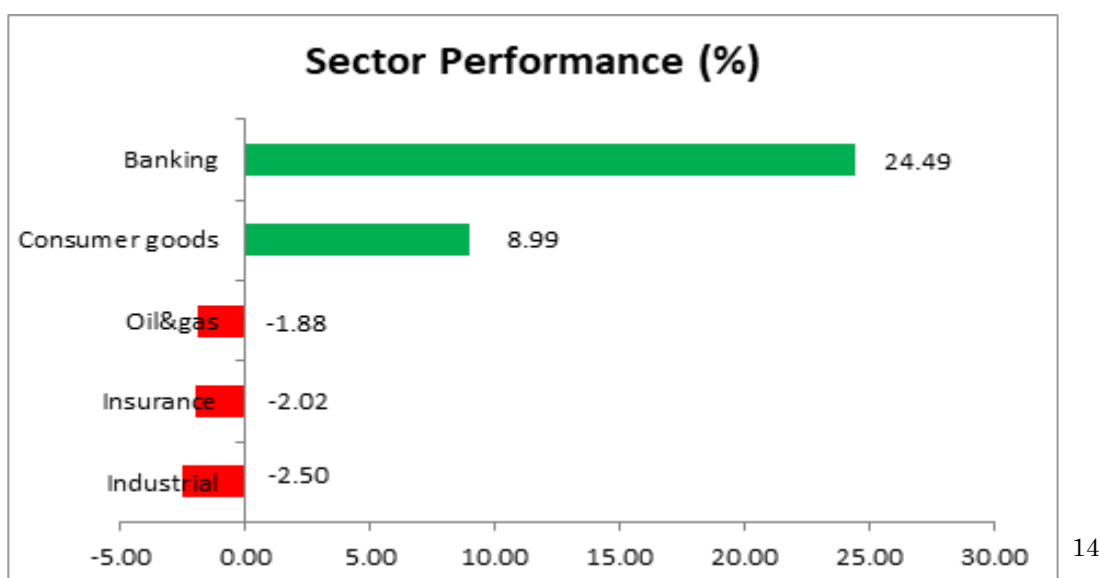
The NSE traded at a price to earnings (P/E) ratio of 6.75x as of April 15th, 6.64% higher than the close of March 31st (6.33x). The market breadth was positive at 1.58x as 41 stocks gained, 26 lost while 96 stocks remained unchanged.



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On the other hand, the market saw a decline in activity level during the review period. The average volume traded fell by 23.65% to 441.11mn units compared to 577.77mn units in the same period in March. The average value of trades also declined by 46.92% to N3.70bn compared to N6.97bn in the corresponding period in March.

<sup>13</sup>NSE, FDC Think Tank



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The performance of the sector indices was mixed during the review period. The banking sector and the consumer goods sectors gained by 24.49% and 8.99% respectively while the industrial sector recorded the highest loss of 2.50% followed by the Insurance sector (2.02%) and oil and gas sector (1.88%).

Dangote Sugar Refinery Plc topped the gainers' list with a 42.70% increase in its share price. This was followed by Oando Plc (41.46%), Lafarge Africa Plc (39.67%), Zenith Bank Plc (39.47%) and Sterling Bank Plc (36.36%).

<b>TOP 5 GAINERS (N)</b>				
<b>Company</b>	<b>1-Apr</b>	<b>15-Apr</b>	<b>Absolute Change</b>	<b>% Change</b>
Dangote Sugar Refinery Plc	8.90	12.70	3.80	42.70
Oando Plc	2.05	2.90	0.85	41.46
Lafarge Africa Plc	9.20	12.85	3.65	39.67
Zenith Bank Plc	11.40	15.90	4.50	39.47
Sterling Bank Plc	1.10	1.50	0.40	36.36

Skyway Aviation Handling Co Plc led the laggards list with a 22.05% decline in its share price. This was followed by Ardova Plc (-18.84%), Cutix Plc (-14.29%), BUA Cement Plc (-13.88%) and Learn Africa Plc (-10.00%).

<sup>14</sup>NSE, FDC Think Tank

<b>TOP 5 LOSERS (N)</b>				
<b>Company</b>	<b>1-Apr</b>	<b>15-Apr</b>	<b>Absolute Change</b>	<b>% Change</b>
Skyway Aviation Handling Co Plc	2.63	2.05	-0.58	-22.05
Arдова Plc	13.80	11.20	-2.60	-18.84
Cufix Plc	1.40	1.20	-0.20	-14.29
BUA Cement Plc	35.30	30.40	-4.90	-13.88
Learn Africa Plc	1.00	0.90	-0.10	-10.00

### *Outlook*

We expect the market to remain volatile in the near term due to low investors' confidence. However, bargain hunting on low-priced stocks could support gains in the near term.

# Corporate Focus: Nestle Nigeria Plc

## Analyst Note

Nestle Nigeria Plc, founded in 1961 and a subsidiary of Nestle S.A. is a Lagos based company known for manufacturing, marketing and distribution of food products. It was publicly listed on the Nigerian stock exchange on April 20th 1979 and operates in the consumer goods sector specifically food and beverages, offering over 2,000 brands ranging from global to local favourites. Products such as baby foods and cereals such as Cerelac, Nutrend, Nan, Lactogen and Golden Morn; dairy products such as Kitkat and Nido; beverage drinks including Milo, Nescafe coffee and Chocomilo; culinary products such as Maggi and Nestle Pure Life.

## Revenue Growth

A 6.67% revenue increase to N284.03bn was recorded in Nestlé's audited full year financial statement for 2019, an affirmation of the company's market leadership. As one of the largest food and beverage companies in Africa, its revenue is sourced from both the domestic market and exports to other African countries like Ghana, Togo, Burkina Faso, Niger, and Guinea. Also, the innovation of new and improved products to meet consumer needs as they arise birthed a few additions to its product portfolio, which enhanced revenue increase

**Analyst Recommendation: HOLD**

**Market Capitalization: N772.84bn**

**Recommendation Period: 365 days**

**Current Price: N975.00**

**Industry: Consumer Goods**

**Target Price: N931.20**

## Strong brand loyalty

In addition to increased revenue, which translated into increased profit supported by reduced operating cost, Nestle has a strong brand loyalty and market leadership. This is because the company's strategy has always been built around creating shared value for all of its stakeholders.

## *Increased PAT and Dividend*

After a strong financial performance for the year ended December 2019, the company proposed an additional N45 per share to the initial N25 per share interim dividend paid earlier. This brings the total dividend to N70 per share, the highest in the history of dividends paid by the company and largely supported by the 6.22% increase in profit after tax to N45.68 bn. There are typically two reasons why companies increase dividend paid. It is either because of the increased profit after tax, which shows that the company is doing well in terms of financial performance and its cash flows have improved. Or as a result of a change in corporate strategy which means the company plans to spend less of its earnings on growth expansion. Knowing that the company is old enough to have stalled growth except it has a breakthrough with innovation, the second point might be the reason. However, a 6.22% increase in PAT can be rest assuring.

## *Industry Snap Shot*

After Nigeria's economic recovery from a long recession that ended in 2017, the sector's performance varied and grew rapidly up until preparations for the 2019 general elections. At a time, the sector was highlighted as the worst performing sector. It grew slowly at 1.1% in the third quarter of 2019 despite being a major beneficiary of government intervention funds and protectionist policies.

Usually the festive period boosts the consumer goods sector performance. Despite ending 2019 on a positive but slow growth, general poor market performance affected this sector very early in the year. And now the coronavirus pandemic is currently making the market bleed and this sector began to underperform falling to its lowest level of 341.99 on the NSE in decades.

With a population of about 200 million, Nigeria has a sizeable consumer goods sector consisting of both indigenous and multinational companies. As the youth and middle class continue to grow, Nigerian retail, industrial and consumer goods sectors will also witness a significant growth. Currently, 16% of Nigeria's GDP is made up of retail and wholesale sales, which are mostly carried

out in the informal market (Open-space market, aboki stands, kiosks, etc) although supermarkets and malls are experiencing increased patronage because of growing urbanization; modern consumers like to shop with convenience.

Big players in this industry are known to have a versatile distribution network and spend significantly to operate efficiently. This has heightened the threat of rivalry in the industry. However, cross border expansion is a part of the numerous opportunities businesses in this industry can think of. Intense competition is a common fact most industry players are aware of and this typically depicts how high rivalry is among players in this sector. Even with the various limiting factors in this sector, companies that invest heavily in research and development of innovative products that meet the needs of consumers are seen to overcome such limitations. This is a typical way for companies to carve a niche for themselves, as the sector still looks very promising post the COVID-19 pandemic.

Nestle Nigeria is a large player in the consumer goods sector both in Nigeria and Africa. The company's presence in Nigeria dates back to 1961 as a local subsidiary of the group. It began with the importation and distribution of products and, after years of hard work and strategic planning the company can boast of two big factories in Nigeria. Where production of wide range of brands and products such as Infant cereals like Cerelac, Nutrend, Family cereal -Golden morn, Beverage drinks -Milo, Confectionaries - chocomilo, season cubes and powders- maggi chicken, crayfish, maggi mix'py, Table water, Coffee- Nescafe 3-in-1, Full cream milk- Nestle Nido.

Local sourcing of raw materials is one of the corporate strategies adopted by the company in order to be less susceptible to currency risk. By 1983, soon after the commissioning of the Agbara factory, many of the imported raw materials used in the manufacturing plants were gradually replaced since they were capable of growing them locally and could develop new product with high local content.

# Nestle Nigeria Plc

Model period ending	check	31 Dec 15	31 Dec 16	31 Dec 17	31 Dec 18	31 Dec 19	31 Dec 20	31 Dec 21	31 Dec 22
Pre-forecast Vs forecast		Pre-forecast	Pre-forecast	Pre-forecast	Pre-forecast	Pre-forecast	Forecast	Forecast	Forecast
Financial year ending		2015	2016	2017	2018	2019	2020	2021	2022
Model column counter	Constant Unit	1	2	3	4	5	6	7	8
<b>Statement Of Financial Position</b>									
<b>Non-current assets</b>									
Property, plant and equipment .	Naira '000	69,148,171	70,171,526	72,377,943	73,365,523	79,393,681	117,302,074	98,386,725	79,615,821
Long term receivables		1,352,196	1,678,251	1,921,232	2,237,105	4,386,059	808,880		
Long term prepayments		-	-	234,170	3,997,477	2,557,090			
<b>Total Non-current Assets .</b>	<b>Naira '000</b>	<b>70,500,367</b>	<b>71,849,777</b>	<b>74,533,345</b>	<b>79,600,105</b>	<b>86,336,830</b>	<b>118,110,954</b>	<b>98,386,725</b>	<b>79,615,821</b>
<b>Current assets</b>									
Inventories .	Naira '000	10,813,960	20,637,750	23,910,303	23,124,020	33,278,945	31,601,840	37,299,724	44,025,119
right of return assets				-	351,995	58,763			
Trade Receivables	Naira '000	24,445,995	24,035,411	31,430,450	42,175,062	65,820,188	52,759,155	62,271,752	73,499,774
Contract Assets					93,179				
Prepayments		525,205	1,711,842	1,791,176	1,228,025	901,518			
Cash at bank and cash in hand .	Naira '000	12,929,526	51,351,152	15,138,854	15,762,036	6,978,071	2,404,153	8,040,848	9,268,765
<b>Total Current Assets .</b>	<b>Naira '000</b>	<b>48,714,686</b>	<b>97,736,155</b>	<b>72,270,783</b>	<b>82,734,317</b>	<b>107,037,485</b>	<b>86,765,148</b>	<b>107,612,324</b>	<b>126,793,659</b>
<b>Total Assets .</b>	<b>Naira '000</b>	<b>119,215,053</b>	<b>169,585,932</b>	<b>146,804,128</b>	<b>162,334,422</b>	<b>193,374,315</b>	<b>204,876,102</b>	<b>205,999,049</b>	<b>206,409,480</b>
<b>Capital and reserves attributable to the company's equity holders</b>									
Share Capital	Naira '000	396,328	396,328	396,328	396,328	396,328	396,328	396,328	396,328
Share Premium		32,262	32,262	32,262	32,262	32,262	25,000	25,000	30,000
Reserve	Naira '000	150,466	126,480	147,236	154,788	123,076	123,076	123,076	123,076
Retained earnings .	Naira '000	37,428,018	30,323,005	44,302,351	49,637,108	45,005,964	44,655,939	44,225,474	43,711,476
<b>Total equity .</b>	<b>Naira '000</b>	<b>38,007,074</b>	<b>30,878,075</b>	<b>44,878,177</b>	<b>50,220,486</b>	<b>45,557,630</b>	<b>45,200,343</b>	<b>44,769,878</b>	<b>44,260,880</b>
<b>Non-current liabilities</b>									
Loans and borrowings	Naira '000	12,530,361	10,384,341	9,564,664	5,921,494	5,516,384	9,202,098	7,887,812	7,387,812
Employee benefits		2,382,213	2,103,744	2,275,921	2,700,673	4,307,927	8,307,927	4,307,927	4,307,927
Deferred tax liabilities .	Naira '000	6,563,548	5,186,338	10,404,871	11,374,268	12,456,944	16,456,944	12,456,944	12,456,944
<b>Total non-current liabilities .</b>	<b>Naira '000</b>	<b>21,476,122</b>	<b>17,674,423</b>	<b>22,245,456</b>	<b>19,996,435</b>	<b>22,281,255</b>	<b>33,966,969</b>	<b>24,652,683</b>	<b>24,152,683</b>
<b>Current liabilities</b>									
Total Trade Payables .		36,661,728	64,662,096	45,668,363	60,384,454	78,400,058	84,101,671	99,265,395	117,163,623
Contract Liabilities				3,387,261	3,858,793	5,974,399	15,550,399	2,000,000	
Refund Liabilities				-	615,211	107,082	729,059		
Bank Overdraft		305,024	154,582	3,714,087	1,393,678	2,736,058	5,965,426	5,169,282	370,522
Current tax liabilities		5,040,468	15,489,634	15,098,670	23,629,987	31,801,369	5,652,699	17,118,185	6,752,235
Loan and borrowings	Naira '000	17,108,803	40,130,375	10,913,246	1,026,458	4,958,904	12,734,536	12,734,536	12,734,536
Provisions	Naira '000	615,834	596,747	898,868	1,208,920	1,557,560	975,000	289,090	975,000
<b>Total Current Liabilities .</b>	<b>Naira '000</b>	<b>59,731,857</b>	<b>121,033,434</b>	<b>79,680,495</b>	<b>92,117,501</b>	<b>125,535,430</b>	<b>125,708,790</b>	<b>136,576,488</b>	<b>137,995,916</b>
<b>Total Liabilities .</b>	<b>Naira '000</b>	<b>81,207,979</b>	<b>138,707,857</b>	<b>101,925,951</b>	<b>112,113,936</b>	<b>147,816,685</b>	<b>159,675,759</b>	<b>161,229,171</b>	<b>162,148,599</b>
<b>Total Equity and Liabilities .</b>	<b>Naira '000</b>	<b>119,215,053</b>	<b>169,585,932</b>	<b>146,804,128</b>	<b>162,334,422</b>	<b>193,374,315</b>	<b>204,876,102</b>	<b>205,999,049</b>	<b>206,409,479</b>





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# Management and Governance Overview

Creating shared value has been a fundamental guide for Nestlé's management team, and it has worked well for them because of their continuous investment in research and innovation towards developing new products that appeal and improve customer satisfaction and loyalty. This has helped the company to sustain its market leadership and make significant impact in its environment.

Nestlé's executives have also successfully positioned the Nestle brand name as a wellness brand, focused on providing the nutritional needs of the consumer. Their ability to continue to deliver value to the customer centers on continuous improvement in line with constant feedback from key stakeholders. Going forward, critical success factors will revolve around reducing customer acquisition costs and acceptability of new innovations (products).

The management of Nestle is under the stewardship of Mr. Mauricio Alarcon, who has robust experience across diverse regions, especially in emerging markets.

Mr. David Ifezuike has served as Chairman of the Board since May 2013. As a previous employee and director, he brings to bear decades of industry experience. Similarly, from the strategic direction of the firm and progress made thus far, it is clear that Mr. David Ifezuike has a good understanding of the business environment and has demonstrated sound leadership helping the firm consolidate on its leadership position in key business segments over the last half decade.



**MD/CEO**

Mr. Mauricio Alarcon



**Chairman**

Mr. David Ifezuike

# Bulls and Bears say

## Bulls say:



- Maintained market leadership in the food and beverage space
- Household brand name in the Nigerian market
- Strategic alliance and support from parent company
- Diversified product offering
- Upward review of minimum wage to boost demand
- Innovative initiatives to improve appeal and customer satisfaction
- Improved operating efficiency

## Bears say:

- Intense competition from other leading players
- Coupled with weak purchasing power
- Limited room for share price surge



## Risk and Outlook

Currently, the main risk is the further spread of the COVID-19 pandemic. A new retail environment has emerged- virtual market with consumers now forced to shop online due to the high risk of virus contagion. This will continue until there is some respite and movement restrictions are removed.

Nestle is the market leader with strong competition from Cadbury (beverages) and Unilever (culinary seasons). It has invested extensively in most input commodities value chain (through its local content policy). The company is marginally exposed to foreign exchange volatility since many of its raw materials are sourced locally.

### *Our Valuation*

Using the Discounted Cash Flow (DCF) methodology, an estimated stock price of N931.20 is 4.49% downside on the current price of N975 per share as of today April 22, 2020. The discount rate (Weighted Average Cost of Capital (WACC)) of 13.5% was derived using a 12.5% risk free rate (FGN 10-year Bond as at March 25,2020), a median sector Beta of 0.74, an after-tax cost of debt of 7.7%, and a market risk premium of 5.7%. The long-term cash flow growth rate to perpetuity calculated is 4%.

Based on our analysis above, and the pandemic effect on the market, a HOLD rating is placed on Nestlé's stock.

DCF Valuation					
N'000	2020	2021	2022		
Total Earnings Before Interest and Taxes	75,070,019	88,605,315	104,581,459	WACC	
Less: Taxes	(22,521,006)	(26,581,595)	(31,374,438)	Debt-to-Total Capitalization	35.6%
EBIAT	52,549,013	62,023,721	73,207,021	Equity-to-Total Capitalization	64.4%
Plus: Depreciation & Amortization Expense	19,359,793	19,415,349	19,470,904	Cost of Debt	11.00%
Less: CAPEX	(700,000)	(500,000)	(700,000)	Tax Rate	30.00%
Change in working capital	20,445,697	(9,979,478)	(17,761,906)	After-tax Cost of Debt	7.7%
Free Cash Flow (FCF)	91,654,503	70,959,591	74,216,019	Risk-free Rate	12.50%
WACC	13.5%	13.5%	13.5%	Market Risk Premium (Rm-Rf)	5.7%
Present Value (PV) of FCF	80,746,823	55,074,985	50,747,257	Beta	0.74
				Cost of Equity	16.7%
				WACC	13.5%
Terminal value @ perpetual growth rate (2020)	2020	2021	2022		
Terminal value as of 2022			811,744,337		
Present value of terminal value	555,052,655			Infinite growth rate	4.0%
				Payout ratio	55%
DCF Calculation	Valuation			Retention rate	45%
PV of explicit period	186,569,065			Return on Invested capital	86%
PV of terminal value	555,052,655			Total Capital	58,768,976
Enterprise Value	741,621,720			EBIT	72,062,046
+ Cash	6,978,071				
- Borrowings	10,475,288				
Equity Value	<b>738,124,503</b>				
Share price	<b>931.20</b>				
Shares outstanding ('000)	792,656				

# Outlook for the next month

The impact of the spread of COVID-19 will continue to constrain activity on both the demand and supply sides of the economy. Non-food markets are expected to close indefinitely as social distancing takes effect. Domestic commodity prices will continue to rise on the back of scarcity fears.

The global oil market is set for an even bigger glut as Saudi Arabia and Russia are set to ramp up oil production in April as part of their price-war. This will outweigh the positive impact of the stockpiling of 30 million barrels of oil by the US government as well as the \$2trn stimulus proposed in an attempt to lift markets and boost its economy. This, in addition to the COVID-19 impact will likely keep Brent prices below \$30pb.

This will ensure that Nigeria's FAAC allocation remains below N600bn – in spite of the exchange rate adjustment to N360/\$ at the official window. The devaluation of the naira to N380/\$ at the IEFX window means higher cost for imports – especially food. This, in addition to scarcity induced by panic buying, will impact March inflation figures negatively.

The continued decline in the external reserves position is expected to continue as lower oil prices persist and the CBN continues to intervene in the forex market. Currency pressures are expected to persist in the parallel market and push the naira down to N410/\$.

The MPC's decision to maintain status quo even as most countries lower rates to stem recession fears is positive for investment flows as its interest rate differential stays the same relative to that of advanced economies. We expect the stock market to extend its bearish streak as negative sentiment persists and foreign investors continue their divestment to safer asset classes – like precious metals.

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