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MPC Surprise Rate Cut:
Limited Impact on Credit Growth

At its penultimate meeting in 2020, the monetary policy committee (MPC) surprisingly lowered the benchmark interest rate by 100bps to 11.5%p.a. from 12.5%p.a. This is the second rate cut in 2020 and the lowest MPR since 2016. The asymmetric corridor between borrowing and placing funds with the CBN has also been expanded to +100/-700bps from +200/-500bps. This means that access to the CBN discount window by the Deposit Money Banks (DMBs) is now cheaper. The standing deposit facility (SDF) will reduce by 300bps to 4.5%p.a. while the standing lending facility (SLF) will fall by 200bps to 12.5%p.a. The CRR and liquidity ratio were left unchanged at 27.5% and 30% respectively.

Contradictions between policy expectations and economic realities

The adoption of a more dovish stance runs contrary to the conventional logic that lower interest rate would fuel inflationary pressures. The assumption that a reduction in interest rates will automatically and immediately translate into output growth and lower inflation undermined the time lag between policy and impact.

According to the EIU, "Tolerance of high inflation by the CBN indicates that the issue will be left largely unchecked over the medium term, as its strategy to boost supply side of the economy plays out to a conclusion – and one that we expect to differ from the MPC's theory".

Headline inflation climbed to 13.22% in August, the highest level in 29 months and is projected to close the year at 14.5% due to higher PMS price and cost reflective electricity tariffs. Rising inflation could dampen investor confidence, squeeze consumer disposable income and reduce aggregate demand.

Shift in the underlying factors driving inflation

It appears that there is a shift in the committee's perspective about the underlying factors diving inflation. The committee attributed the build-up in inflationary pressures to structural rigidities and supply shocks, downplaying the exchange rate pass through and transmission effect between M2 growth and prices. The MPC had in the past ascribed the rise in the general price level to exchange rate pass through and growth in money supply. Moreover, the structural bottlenecks had existed in the past and are unlikely to be addressed in the short to medium term, even with an expansion in credit.

Implications

Limited impact on credit growth

The CBN's dovish stance is expected to reduce cost of funds but is likely to have a limited impact on credit growth. This is due to the high level of risk aversion by Nigerian banks. Since the last rate cut in May'20, credit to the private sector grew in nominal terms but the rate of growth slowed to 6.94% in August compared with 7.47% in May.

Interest rate-inflation differential in favour of the US

Lower interest rate amid rising inflation increases the interest rate-inflation differential in favour of the US. This heightens the risk of capital flight, which will further increase the pace of external reserves depletion. Also, Nigeria being an import dependent economy stands the risk of higher import prices due to a stronger dollar. This will negatively impact the country's balance of trade and terms of trade levels. The CBN's ability to support the naira is undermined and hence we could experience some exchange rate volatility.

	Inflation (%)	90-day T/bills (%)	Inflation-interest rate differential (%)
Nigeria	13.22	1.2	12.02
US	1.3	0.12	1.18

Monetary easing to reduce marginal propensity to save (MPS)

The 100bps cut in MPR means a further 10bps reduction in the minimum interest rate on savings. This at a time when inflation is galloping implies that the negative real rate of return on savings will widen. The impact of this will be a reduction in the marginal propensity to save, which will translate to a higher marginal propensity to consume (MPC) and could stoke inflationary pressures.

Outlook

We do not expect a significant change to the monetary policy stance again this year. The committee will continue to monitor the impact of the rate cut and other policy pronouncements on economic growth and prices. However, a further spike in inflation could force the MPC to reverse its current monetary stance and tilt towards a tighter monetary stance in 2021.

Nigeria, South Africa and Ghana: Pre-covid, covid and post-covid

Nigeria, South Africa and Ghana are three of the largest economies in Sub Saharan Africa (SSA) with a collective economic size that is 49.37% of the region's GDP. They are also the most affected by the coronavirus, accounting for 66.39% of total infections and 69.89% of total fatalities in the region. The countries, which have tried to stay afloat prior to the pandemic were all brought to their knees at the wake of the health crisis, although Ghana appeared to be in a better economic state than the other two (SA was already in a recession and Nigeria was growing abysmally low at 1.87% in Q1'2020).

In Nigeria, we expect stagflation to continue in the coming quarters, with inflation rate still at 13.22%, contracting growth rate of -6.1% (the deepest since 1983) and a high unemployment rate of 28%. The fiscal stimulus expected to cushion the impact of the pandemic will be an inadequate counterforce, given the budget constraints. Consumer price inflation is also expected to rise above 14% in 2020, from 11.4% post-covid. The high inflation in Nigeria is structurally as a result of the exchange rate restrictions on the import of several commodities coupled with supply constraints in the middle belt. This implies that further currency depreciation or adjustments would keep inflation elevated post-covid.

Key Indicators

		Pre-covid (2019)	covid (2020)	Post-covid (2021)
Nigeria	GDP growth (%)	2.2	-5.4	2.6
	Inflation (%)	11.4	14.2	12.4
	Exchange rate (N/$)	306.4	378.4	449.6
South Africa	GDP growth (%)	0.2	-8.0	3.5
	Inflation (%)	4.1	5.0	4.3
	Exchange rate (R/$)	14.44	17.12	17.80
Ghana	GDP growth (%)	6.1	-4.1	5.9
	Inflation (%)	7.6	11.2	8.3
	Exchange rate (Ghc/$)	5.21	5.65	6.15

Unlike Nigeria that started the year on the right foot, South Africa started with a recession. As if the recession in 2019 wasn't bad enough, the pandemic deepened the recession.

South Africa's economy slumped into a second recession contracting more than projected in Q4 as power cuts weighed on output and business confidence. For the full year, expansion was 0.2%, which was lower than the central bank's projection. Based on an average rand-dollar exchange rate of 14.44 for the year, GDP was $352 billion.

As a result of South Africa's weak growth numbers, the central bank lowered the benchmark interest rate at its MPC meeting in March, before maintaining status quo.

Inflation rate is expected to rise to 5% in 2020, from 4.1% in 2019 (a multi-year low), but price increase will remain modest. The reason for higher inflation in 2020 will be rand depreciation, higher electricity tariffs and possible tax increase.

In Ghana, the next presidential elections are due in December 2020 and there are growing tensions between the two main parties, the NDC and the NPP. More importantly, the advent of the crisis changed the nature of politicking for both parties.


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In terms of the number of infections, Ghana is SSA's third most affected nation (behind South Africa and Nigeria), which reflects the government's policy of widespread testing. Due to the pandemic, we expect a contraction of 4.1% in GDP in the year.

In line with the sharp downturn in economic activities, we expect average inflation to remain elevated in 2020, averaging 11.2% (from 7.6% in 2019). This reflects a weaker currency (Ghc5.65/$), which we expect to continue as the fiscal deficit widens and investor uncertainty mounts ahead of the December election. Inflation will then moderate in 2021, to 8.4%, as disruptions to supply chains fade and domestic demand remains weak.

Conclusion

The projections indicate that recovery will be different for countries and this will be based on government policies earmarked to stimulate the economy. For instance, the IMF forecasts that Ghana's economy will be the fastest growing of the 3 economies. While Nigeria and South Africa's economy will contract by -5.4% and -8% respectively due to the pandemic, Ghana's GDP is forecast to expand to 1.5%.

Fear of lower output looms as excessive rainfall stalls cocoa harvest

Nigeria is likely to witness a sharp fall in its cocoa output in the 2020-21 harvest season due to excessive rainfall in the South Western states – predominantly in Ondo and Ogun. Early harvest of the main crop, which typically commences in September-October, has been halted as farmers express grief over the lack of sunshine to dry cocoa pods after being harvested. In addition, a possible outbreak of the black pod disease, which thrives during the wet season, is also a major threat to output. The disease, if left unchecked could damage up to 40% of Nigeria's annual cocoa output.

Cocoa is Nigeria's largest agric export commodity, accounting for 1.46% of total exports and 41.38% of total agric exports in Q2'20. Approximately 70% of the country's annual production (330,000 tons in 2018) of the commodity is grown in the South West. The major producing states are Ondo, Ogun, Osun, Ekiti and Oyo.

Impact

The anticipated fall in cocoa production at a time of dwindling oil prices would further put a strain on government revenue. It could also undermine the government's effort at achieving food security in Nigeria.

In a bid to achieve food security and sufficiency, the CBN has directed banks to increase their exposure to the agric sector from 4% currently to 10%. The president has also directed the CBN to suspend forex for food and fertilizer imports. Increased credit allocation to the agric sector is expected to provide huge support to the sector, improve productivity and boost domestic output. The expected boost in food production will reduce food imports and lower food prices. Nigeria's food import bill currently stands at $20 billion annually.

Specifically, increased access to funds could avail cocoa farmers the opportunity to put in place the necessary storage and drying facilities, which will help to guard against subsequent shortfalls in output.

The Untapped Potential of the Nigerian Film Industry

Amongst the many juggernauts within the Nigerian entertainment industry, one that stands out is the film industry, otherwise known as Nollywood. It is the world's second largest movie industry by volume, surpassing Hollywood and coming just short of India's Bollywood. Nollywood currently produces more than 2,000 movies and TV series each year, most of them in Yoruba, Hausa, Igbo and English, the most widely spoken languages in Nigeria. This, however, does not mean that Nollywood surpasses both Hollywood and Bollywood in terms of production quality or return on investments. In fact, the highest grossing Nollywood movie, *The Wedding Party* (2016) made just $1.176 million (N453mn). It was dwarfed by India's *Dangal* (2016), which grossed about $296 million (N113.8bn).[1, 2] Nonetheless, in 2016, Nollywood contributed 2.3% (N239 billion) to Nigeria's GDP, and PwC identified it as one of the priority sectors in the Economic Recovery and Growth plan of the Federal Government of Nigeria.[3] Despite its successes in recent years, it is evident Nollywood suffers from a myriad of issues, most notably, a lack of investment, piracy and distribution challenges, which date back to the industry's beginnings. If Nollywood is to live up to the potential predicted by PwC it needs to look to its big brothers in film, Bollywood and Hollywood for creative investment solutions, piracy enforcement and innovative distribution that leverages Nigerians' love for a home video through the streaming opportunities available today.

[1]Akanksha Bhatia. n.d. "List of Top 15 highest-grossing Bollywood Movies of all time". SchoopWhoop. https://www.scoopwhoop.com/entertainment/highest-grossing-indian-films-of-all-time/

[2]Augoye, Jayne. 2020. " 'Wedding Party 1' named highest-grossing Nollywood movie of the decade". *Premium Times*. https://www.premiumtimesng.com/entertainment/nollywood/371619-wedding-party-1-named-highest-grossing-nollywood-movie-of-the-decade.html)

[3]Osinubi, Femi. 2017. "Spotlight – The Nigerian film industry". PwC Nigeria. https://www.pwc.com/ng/en/assets/pdf/spolight-the-nigerian-film-industry.pdf.

History and Pressing Issues

Nollywood, as we know it today, has its origins in the late '90s after the release of *Living in Bondage* (1992). This was the first Nollywood blockbuster released straight to video and the first movie to show how lucrative film making directly on video could be. The movie's release ushered in the home video boom of the Nigerian film industry, in which many aspiring directors and producers turned to direct-to-video production methods in order to cut costs. While this proved effective in terms of quantity, the quality of most of the films was lacking. As independent film producer Ejike Nwankwo explained to the *Vanguard*, "Films can be produced with as little as $10,000. The low budget film makes it possible for us to shoot and complete production as quickly as possible, sometimes within a month or less. But sadly, it affects the quality of productions as everything is hurriedly done."[4]

Despite the initial success of movies during the home video era, the low quality quickly left people disillusioned, to the point where many Nigerians refused to support Nollywood. For many people, the inability to produce films on the same caliber as Hollywood blockbusters discouraged them from supporting the movie industry referring to the movies as a 'disgrace to the Nigerian people'.[5]

Low quality movies cannot only be attributed to low budgets and rushed productions. Inadequate infrastructure is another problem which plagues many film studios, as they are chronically underfunded, and piracy remains a major concern for home videos. Pirated versions of films often appear in circulation just days before their actual release dates. This undermines profits and the ability for producers to fully pay their cast and crew.

In recent years, a major shift in the method of film production has begun to materialize, the shift from home video releases to theatrical cinema releases. In the early 2000s, Nigeria experienced a major growth in cinemas due to companies such as the Silverbird Group that launched various modern cinemas across major cities in Nigeria. These cinemas are mostly situated in affluent areas and districts, and started with the Silverbird Galleria in Victoria Island, Lagos in 2004. With Nigeria's population nearing 200mn, as at 2019, there are only 68 cinema chains and about 218 screens.[6]

[4]McPhilips Nwachukwu. 2020. "The Industry called Nollywood". Vanguard. https://www.vanguardngr.com/2012/06/the-industry-called-nollywood/. Paragraph 20.
[5]Affi White. n.d. "Nollywood: The History and Development of Nigerian Cinema". https://affiwhitecontentproject.weebly.com/negative-affects-on-nollywood.html
[6]2019. "Nigeria Box Office Year Book, 2019". http://books.filmhouseng.com/books/jahx/#p=6

This is where the problem arises; these cinema chains and screens are almost solely available in the main cities of Lagos, Abuja, Port Harcourt and Kano. It is very rare to experience a vibrant cinema culture in other parts of Nigeria, not because the people in these parts hate films, but because investors do not believe they will get a high enough return on investment.[7] For the cinemas that do exist, they are primarily used to host foreign movies, as domestic movies fail to attract significant audiences. Those perennial problems of quality and piracy continue to haunt Nollywood as it attempts to expand into the international cinema market.

Hollywood and Bollywood – The Big Brothers

When comparing costs of film production in Hollywood the average budget ranges from $70mn - $100mn. A premiere blockbuster can cost between $200mn - $400mn.[8, 9] Bollywood's budgets also drown out Nollywood, even if they are well below Hollywood at an average of $200,000 - $700,000. Though Nigeria has recorded improvements in its film budgets in recent years, the end results are lacking compared to the results of the bigger industries. Attracting investors through corporatization of film studios, much like how Bollywood studios UTV and Eros, is a sure way of improving budgetary processes as these studios handle the production, distribution and marketing of their content (thus limiting the tendency for directors and producers to exceed their budgets).

[7]Rejoice Abutsa. 2019. "How successful is Nollywood in Comparison to Bollywood and Hollywood and other film industries?". Quora. https://www.quora.com/How-successful-is-Nollywood-in-comparison-to-Bollywood-and-Hollywood-and-other-film-industries
[8]Parlay Studios. 2017. "Feature Film Breakdown". The Take. https://parlaystudios.com/blog/feature-film-budget-breakdown/#:~:text=The%20Average%20Cost%20to%20Produce,between%20%2470%20and%20%2490%20million.
[9]Highsnobiety. 2020. "The 10 Most Expensive Hollywood Movies Ever". https://www.highsnobiety.com/p/most-expensive-hollywood-movies/
[10]Divij Joshi. 2017. "With Internet Archive Ban, Bollywood's Fight Against Piracy Threatens Online Freedom Again". The Wire. https://thewire.in/business/internet-archive-bollywood-piracy

To combat piracy, a group of 30 entertainment companies, including big names such as Netflix, HBO, and NBCUniversal joined forces and established the Alliance for Creativity and Entertainment (ACE), which would allow IP holders involved to pool resources to conduct research and work closely with law enforcement to find and stop pirates from stealing movies and TV shows. A similar establishment between private companies like Silverbird, FilmOne and Blue Pictures could benefit the Nigerian entertainment sector. Another way Nigeria could curtail piracy – albeit with the risk of limiting one's online freedom – is by introducing online censorship for piracy sites. India did this in 2017 after the Madras high court ordered approximately 2,650 websites to be blocked nation-wide as an interim measure against the infringement of copyright of certain films.[10]

Lastly, Nollywood needs to address the issue of distribution. It needs to capitalize on its fledgling international recognition. The global powerhouse, Netflix, has set up partnerships with Nigerian production companies, releasing "Lionheart" in 2018 and teaming up with Ebony Life studios to embark on a string of Netflix-branded projects. However, these efforts are not enough; more distribution channels need to be established both domestically and abroad in order to attract more viewers and potential investors, and to limit piracy. Other than forming partnerships with foreign distribution services, producers and stakeholders should promote Nigeria's domestic streaming services such as Showmax, Filmhouse One and IrokoTV thus improving domestic demand.

The Nigerian movie industry is a potential gold mine waiting to be tapped, and though steps are being taken to unlock this potential, they barely scratch the surface. Nigerians must look towards the advanced film industries, their issues and how they attempt to solve them, and take note of what needs to be done to improve Nollywood.

Nigerian Airports – Lessons from Singapore!

Airports have become fully integrated in the economic and social strata of various countries. It plays an important part in air transport system and is very significant to increasing the quality of life of regional and local communities, directly participating in wealth creation [11]

Global & domestic aviation industry in distress

This year, the global aviation sector could contract by approximately 55% and load factor by 41%. This is the consequence of worldwide lockdowns and restrictions on domestic and international air travel. The entire sector could lose over $84bn in 2020 with revenues falling by over 50% compared to 2019. Profit levels could also contract by 20.1%.[12]

Of all the transportation services in Nigeria, air transport took the biggest hit at this time of the pandemic. It contracted 57.38% in Q2'2020 from 5.68% in Q1'2020. Domestic and international flights have now resumed which points to a slow recovery in the sector. However, passenger traffic could still be low as individuals are pessimistic about contracting the virus and revenues will remain thin compared to the pre-COVID levels. One thing is certain - things will not remain the same

[11]Hengsheng Gu (2019). "Airport Revenue Diversification" Journal of Management Science & Engineering Research. The University of Sydney, Australia

[12]IATA Press Release, June 9, 2020. "Industry Losses to Top $84bn in 2020" International Air Transport Association (2020). https://www.iata.org/en/pressroom/pr/2020-06-09-01/

Nigerian airports are still sub-optimal

Nigerian airports are still not up to global standards. In addition, when compared to peer countries like South Africa and Ghana, it is evident that the country still has a long way to go in terms of airport infrastructure. There are still a number of persisting challenges for Nigerian airports ranging from poor management and administration, to maintenance, structural and regulatory bottlenecks to mention a few. A recent survey revealed that the conduct of some officers (immigration and customs) and careless handling of luggage are top pain points of travelling through Nigerian airports. In addition, travelers have complained over time that the Nigerian airport experience does not measure up to acceptable global standards.

The way forward

The Singapore model

In the past 40 years, the Changi airport has developed and expanded to become the best airport in the world. Through consistency and strict compliance to development plans, the airport has expanded from one to five terminals. In addition, there has been adequate provision of other vital support facilities like aircraft engineering support, in-flight catering services, fire stations and utilities. Furthermore, other sensitive divisions like security and transport and customer services have remained top priority at the airport. The aesthetics of the airport (travel and leisure theme), presence of cinemas, restaurants and shopping complexes has not only increased passenger traffic but also revenue. In 2019, passenger traffic was over 68 million people. Travelers often commend the airport experience and ease of navigating the airport.

Airport concessioning has also contributed immensely to the efficient organization of the airport. The effective management practices by the Public Works Department of the Changi Airport Development Division supported the fast growth and development of the airport. Changi Airport was corporatized and came under a new company, Changi Airport Group, when the Civil Aviation Authority of Singapore (CAAS), which had managed the airport for 25 years, was restructured into two separate entities – Changi Airport Group, which oversaw airport operations, and the restructured CAAS, which was involved in regulatory issues.[13]

[13]Tan Bonny, "Changi Airport" Singapore Infopedia

Lessons for Nigeria

- There is need for increased investment towards airport infrastructure as it will help reduce average costs and increase revenue. For example an expansion of airport parking spaces could increase income generated from parking tickets.
- Public-private partnership will attract more investment. It will also help in terms of management, income generation and accountability. The presence of private ownership will intensify the need to boost revenue and profit.
- Airport aesthetics could also be a tourist attraction and this could increase passenger traffic and in turn revenue.
- Effective implementation of development plans cannot be over-emphasized.

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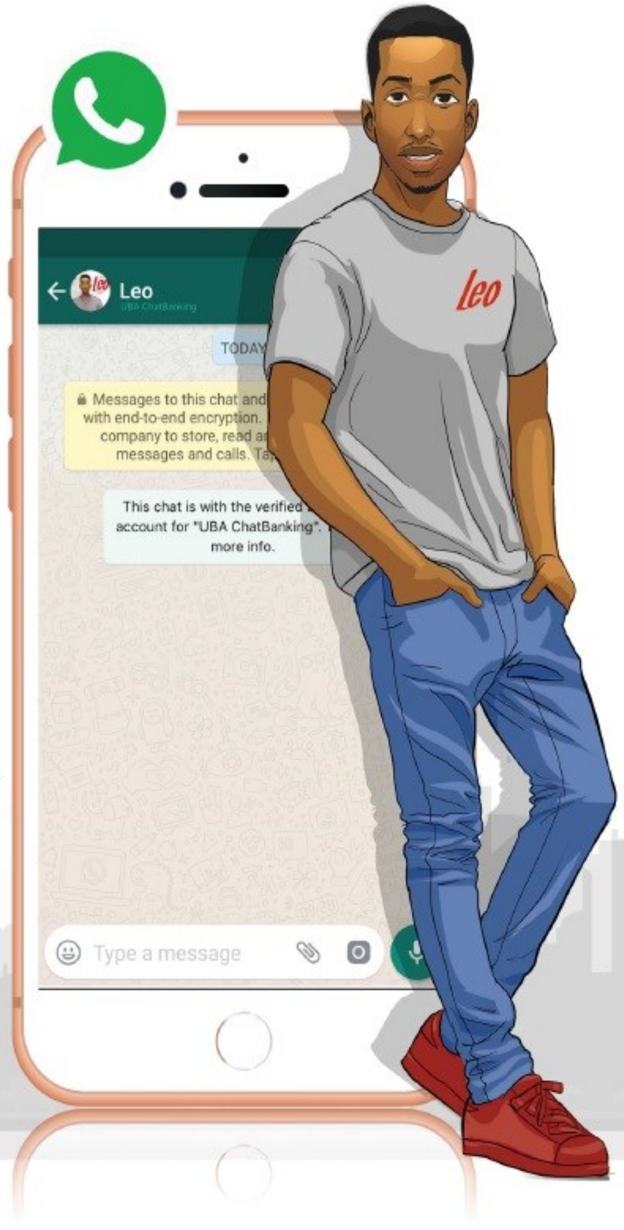

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How has trade survived covid-19?

Global Perspective: Culled from the Economist

Better than during the global financial crisis

In Quentin tarantino's "Kill Bill: Volume 2", an action drama, the protagonist, played by Uma Thurman, punches her way out of a coffin. Global trade in goods has performed a similar death-defying stunt during the covid-19 pandemic. In April, things looked dismal. Some predicted global trade would slump by more than 30% this year, compared with 2019. But after a gut-wrenching spring, trade volumes recorded their biggest monthly rise on record in June, the last month of available data. Oxford Economics, a consultancy, predicts that in 2020 as a whole, volumes may drop by 10%.

This resilience has defied recent experience, as well as expectations. In 2009, when global GDP fell by 0.1% in the final year of the financial crisis, trade plunged by a whopping 13%. This year the IMF forecasts that global GDP could fall by 4.9%, ie, 50 times more than in 2009. So why will the hit to trade probably be smaller?

After the financial crisis trade volumes fell much further than GDP mostly because people stopped buying heavily traded durable goods, such as cars. But in the current crisis, untraded domestic services have been harder hit than they were back then. Going to the cinema or a restaurant halted during lockdown. Buying an imported fridge did not. That has made the drop in trade relative to GDP smaller.

Moreover, the robustness of the world's production apparatus has underpinned trade flows. Covid-19 froze supply chains, but in Asia at least they swiftly started to thaw. According to Simon Evenett of the University of St Gallen in Switzerland, the number of trade restrictions applied on medical goods and medicine since the start of the crisis peaked in April, and has since fallen by 15%.

Even more importantly, lockdowns were lifted more quickly than expected, allowing exporting powerhouses like China and Germany to reopen factories and boost output.

Pandemic-induced demand gave trade in some products extra pep. America's imports of protective equipment tripled between March and July, calculates Panjiva, a trade-data company. Covid-related products including computing equipment for home-working has accounted for the majority of China's year-on-year export growth in each month since June. Eytan Buchman of Freightos, an online marketplace, reports that ocean-freight prices are surging for routes between America and South-East Asia, partly because of "near-frantic" e-commerce offerings by small businesses.

Policymakers have played a pivotal role in the trade revival. Monetary and fiscal firepower was bigger and faster than trade experts had expected. Central-bank liquidity measures kept trade finance flowing better than it did during the financial crisis, says Jennifer McKeown of Capital Economics, a research outfit.

Although the trade performance is cause for relief, no one should declare victory yet. A second wave of lockdowns, or overhasty efforts to curtail economic stimulus, could derail the recovery. The value of exports from South Korea dipped in August relative to July, as did those of China after adjusting for an artificially depressed base in 2019. Robert Koopman, chief economist of the World Trade Organization, which oversees global trade, doubts there will be a sustained v-shaped recovery.

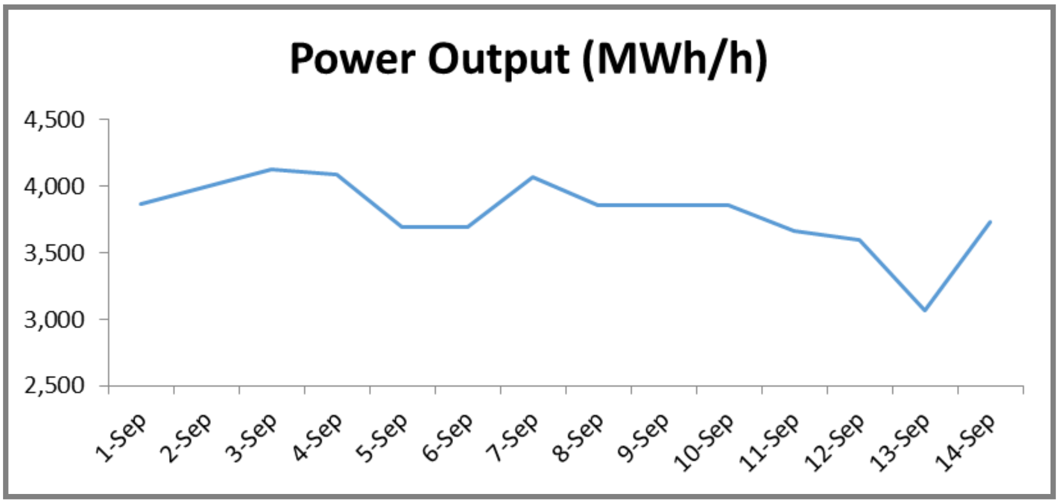
Overlaying this is a concern about the lingering unevenness of trade. Brad Setser of the Council on Foreign Relations, an American think-tank, says that the trade slump has shrunk the gap between most countries' imports and exports, reducing imbalances. Yet there have been two standout exceptions. The first is China, whose rapid reopening has sent its exports of goods surging to a level last seen before the Sino-American trade war—almost $60bn higher than imports in August. The second is America, whose policies to stoke demand have had the side-effect of causing its trade deficit to increase further—to around $80bn in July.

This imbalance is ominous. Although the so-called Phase One trade deal between America and China was meant to prop up American exports to China, so far it has disappointed. Meanwhile, President Donald Trump is haranguing China ahead of elections in November. Trade may not have performed as badly as many feared. But it still has an alarming ability to pack a Thurman-esque punch.

Macroeconomic Indicators - September (1st – 15th)

Power Sector

During the review period, an average of 3,787MWh/h power output was sent out from the national power grid. This is 5.96% lower than the average of 4,027MWh/h recorded in the first half of August. Gas remains the dominant constraint to power generation primarily in Odukpani NIPP and Alaoji NIPP plants. Total constraint during the period was 35,703MWh/h, resulting in a revenue loss of N17.14billion (N205.68billion annualized).



[14]

Outlook

Water constraint remained subdued in the review period and we expect this trend to continue in the near term owing to delayed rainfalls. This will boost hydro-generated power and improve power output in the near term. Also, the cost reflective electricity tariffs, which kicked-in on September 1 is expected to spur investment in the power sector and improve power supply in the long term.

Impact

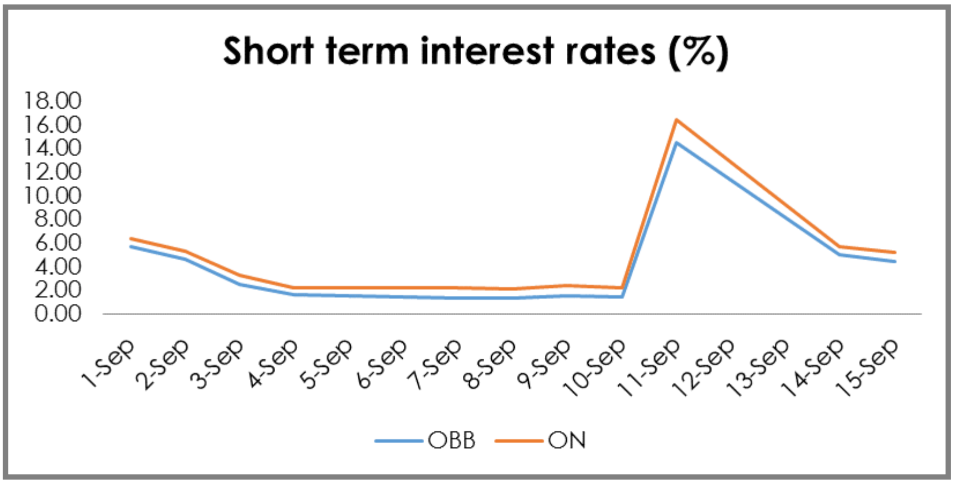
An increase in power supply implies that companies will source less for alternative energy, pushing down their operating costs, consequently increasing their margins.

[14]**FGN, FDC Think Tank**

Money Market

The average opening position of banks rose sharply by 36.45% to N414.19 billion in the first half of September from N303.55 billion in the corresponding period in August. This was in spite of banks' funding for the CBN's retail forex auction during the period and a net OMO outflow of N100 billion. While there were no OMO maturities in the period, OMO bills issued amounted to N100 billion.

The increase in market liquidity resulted in the decline in short-term interbank rates. Average NIBOR (OBB/ON) fell by 402bps to 4.44% in the review period from 8.46% in the corresponding period of August. OBB and ON rates reached a period high of 14.50% and 16.50% respectively on September 11th, before declining sharply to close the period at 4.40% and 5.20% respectively.



[15]

There was a primary market auction on September 9th worth approximately N128.05 billion which was oversubscribed by 104.92%. T/bill yields declined across all tenors by an average of 20bps. On the other hand, there was a mixed movement of yields at the secondary market. Yields fell for the 91-day and 364-day tenors and increased for the 182-day tenor.

Primary Market

T/bills Tenor	Rate on Aug 26th (% pa)	Rate on Sept 9th (% pa)	Direction
91	1.15	1.10	↓
182	1.80	1.55	↓
364	3.34	3.05	↓

Secondary Market

T/bills Tenor	Rate on Sep 1st (% pa)	Rate on Sep 15th (% pa)	Direction
91	2.37	1.50	↓
182	1.00	1.32	↑
364	3.08	2.50	↓

[16]

[15]CBN
[16]FDC Think Tank

Outlook

We expect a decline in market liquidity in the near term due to funding for the CBN's forex sale to BDCs on resumption of international flights.

Impact

A decline in market liquidity will push up short-term interbank interest rates.

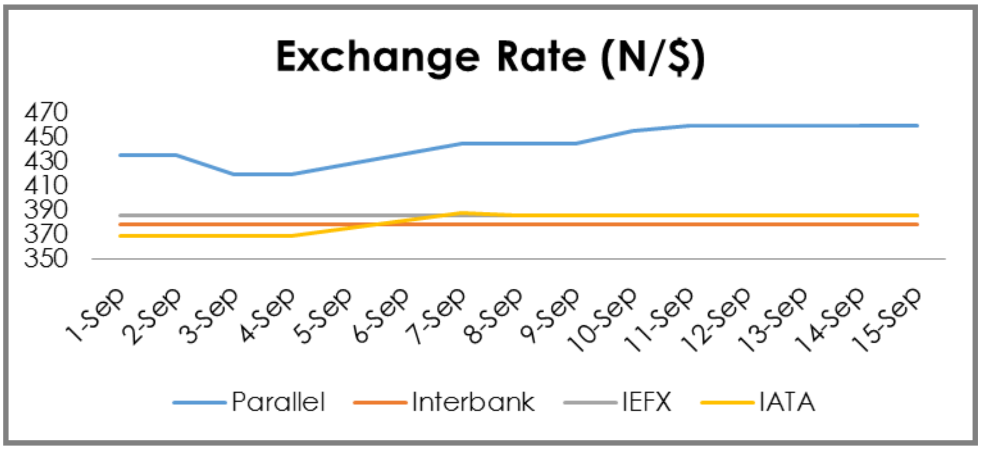
Forex Market

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

The resumption of international flights on September 5 resulted in the dumping of foreign exchange currencies by jittery speculators, which strengthened the naira at the parallel market. The currency appreciation was however short-lived as demand pressures resurfaced and the currency lost 5.43% and closed the period at N460/$ at the parallel market. The naira traded flat at N379/$ at the interbank market in the review period.

At the IEFX window, the naira traded within a tight band of N386/$ - N386.25 in the first half of September and closed the period at N386/$. Activities increased at the window evidenced by the 135% increase in total turnover to $872.68 mn during the review period from $371.30 mn in the corresponding period of August.



[17]

[17]FMDQ, CBN, FDC Think Tank

Outlook

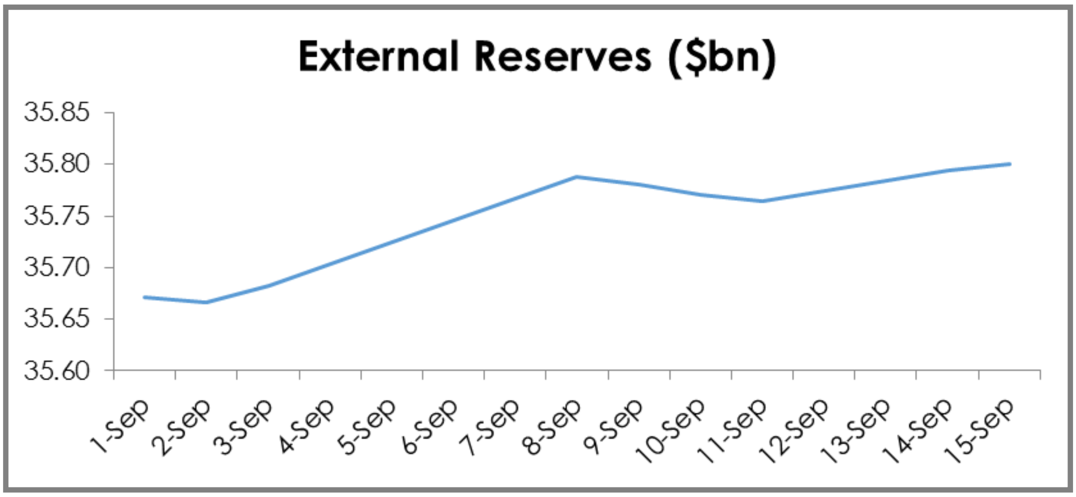
The CBN's retail forex auction and weekly forex allocation to BDCs are unlikely to stem forex demand pressures due to the growing forex backlog and resumption in more economic activities. This will continue to impact negatively on the exchange rate.

Impact

The impact of increased forex demand could outweigh the effect of the CBN's $20,000 weekly allocation to BDCs leading to a weaker exchange rate. This will negatively affect industries that are highly dependent on imported inputs.

External Reserves

During the review period, external reserves recorded a choppy movement. At the start of the period, gross external reserves increased for four consecutive days before falling to $35.78billion on September 9. By the end of the period, reserves recorded a cumulative gain of 0.36% ($130million) to close at $35.8billion. Currently at $35.8 billion, Nigeria's external reserves balance can fund 8.91 months of import cover compared to 8.88 months on September 1st.



[18]

Outlook

Increased forex supply from the CBN coupled with lower oil prices will lead to depleting external reserves.

Impact

The stability of the exchange rate is a function of the robustness of Nigeria's external buffers. Depletion in the external reserves balance will limit the CBN's ability to defend the currency.

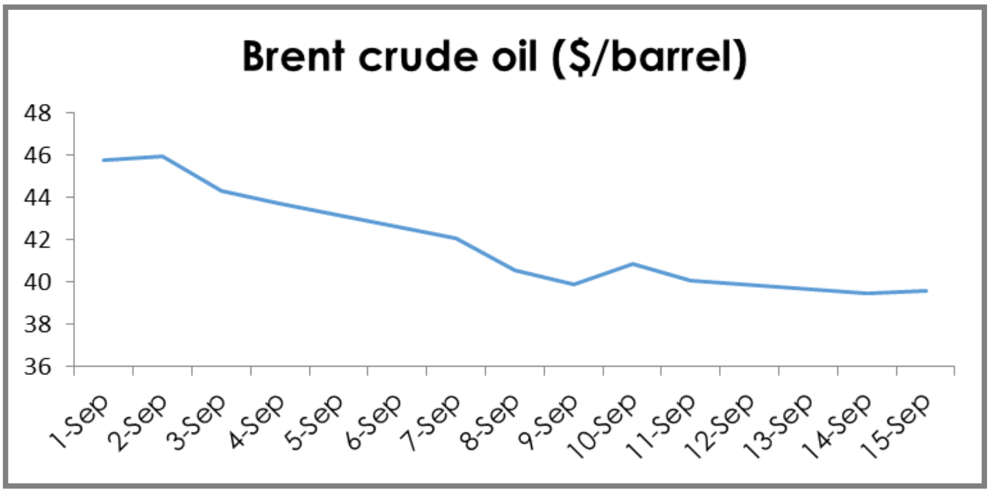
[18]CBN

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

During the period, oil prices were volatile, peaking at $45.98pb on September 2nd. Oil prices on average declined by 6.46% to $42.02pb from an average of $44.92pb in the first half of August. This was on the back of renewed demand concerns due to a surge in Covid-19 cases in countries such as the US and India.



[19]

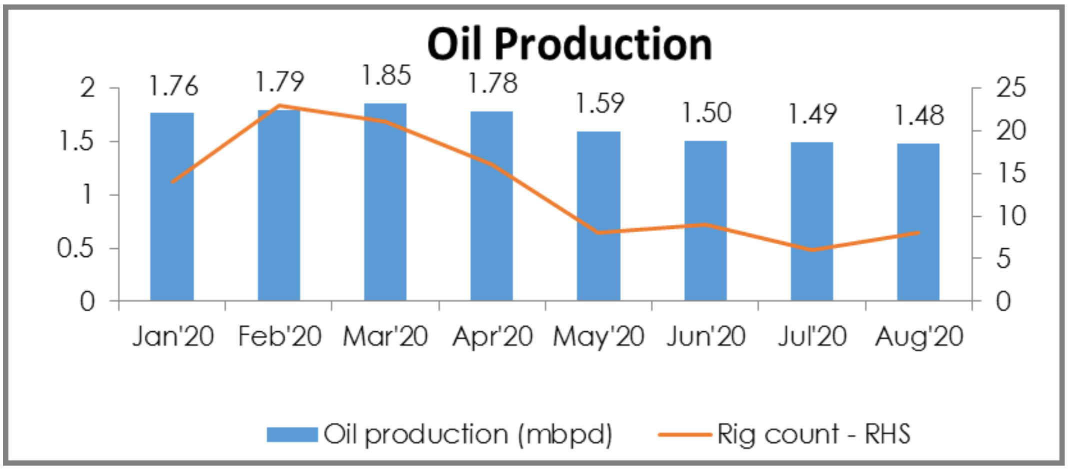
Outlook

We expect oil prices to maintain the bearish trend in the near term driven by poor global oil demand outlook. The non-compliance of member countries such as Nigeria to their OPEC quota coupled with rising US inventory levels would also keep prices depressed in the short term.

Oil production

Nigeria's oil production was 1.48mbpd in August, down 0.67% from 1.49mbpd in July. This was in spite of an increase in the oil rig count to 8 in August from 6 in July. Meanwhile, OPEC's crude oil production rose by 0.76mb/d to an average of 24.05mbpd in August. Oil output increased in Saudi Arabia, UAE, Kuwait, Algeria and Angola, while it fell in Iraq.

[19]Bloomberg



[20]

Outlook

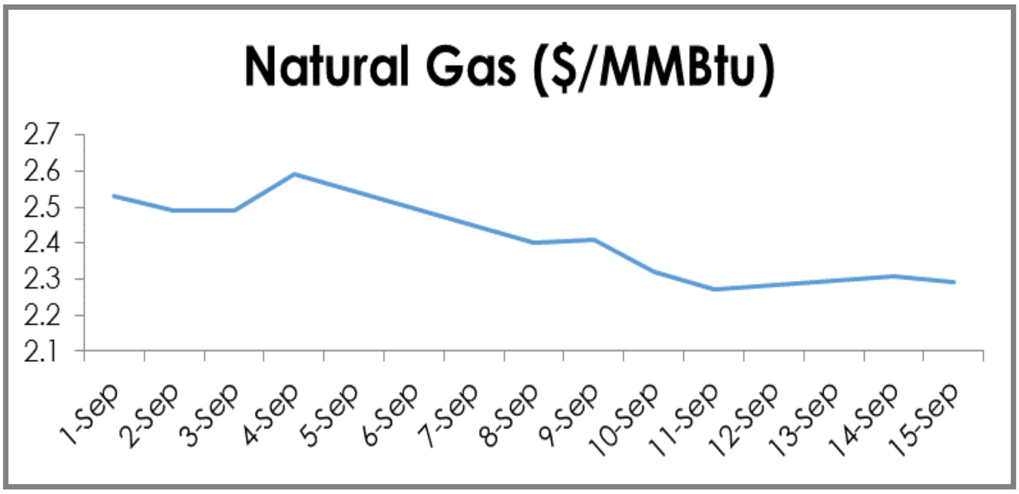
Nigeria's current oil output is currently 4.96% above the country's OPEC quota of 1.41mbpd. This is likely to receive pushback from OPEC+ as Nigeria continues to produce more than its quota. Therefore, oil production could decline in subsequent months.

Impact

Nigeria remains more oil production sensitive than oil price sensitive. Thus, a decline in oil output could threaten the country's oil revenues, fiscal and external buffers. This would have a negative impact on proxies such as FAAC allocation.

Natural Gas

The average price of natural gas during the review period was $2.41/mmbtu, which is 10.05% higher than the average price of $2.19/mmbtu recorded in the first half of August. The increase in price was in spite of subdued LNG demand amid cooler weather conditions in the US.



[21]

[20]OPEC, FDC Think Tank
[21]Bloomberg

Outlook

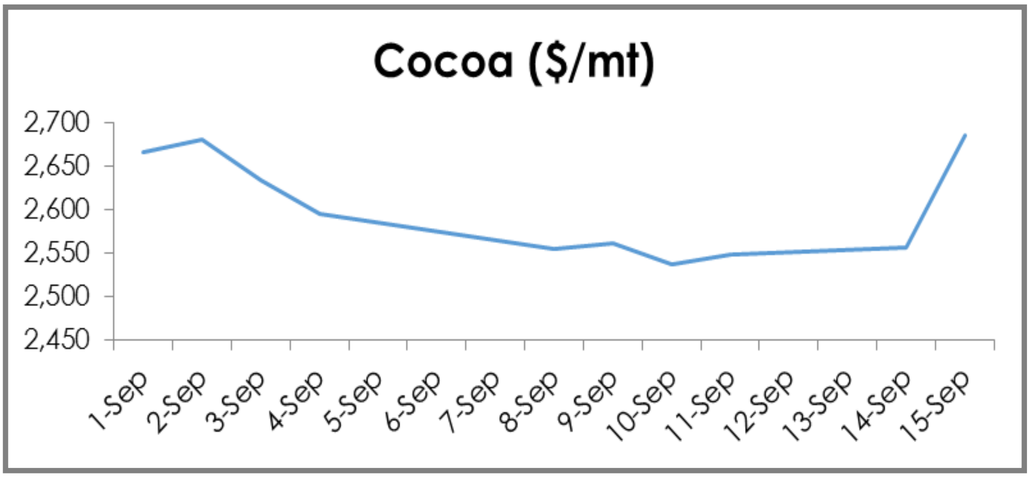
Natural gas prices are expected to decline in the coming period driven by lower LNG demand.

Impact

A decrease in the global price of natural gas will negatively affect Nigeria's LNG export earnings as the commodity is a major export for Nigeria, accounting for approximately 13%[22] of the country's export revenue.

Cocoa

Average cocoa price increased by 5.22% to $2,602/mt in the review period from an average of $2,473/mt in the corresponding period of August. The increase in price was buoyed by projections of lower global cocoa supply.



[23]

Outlook

We expect cocoa prices to decrease in the coming days driven by improved global cocoa supply outlook.

Impact

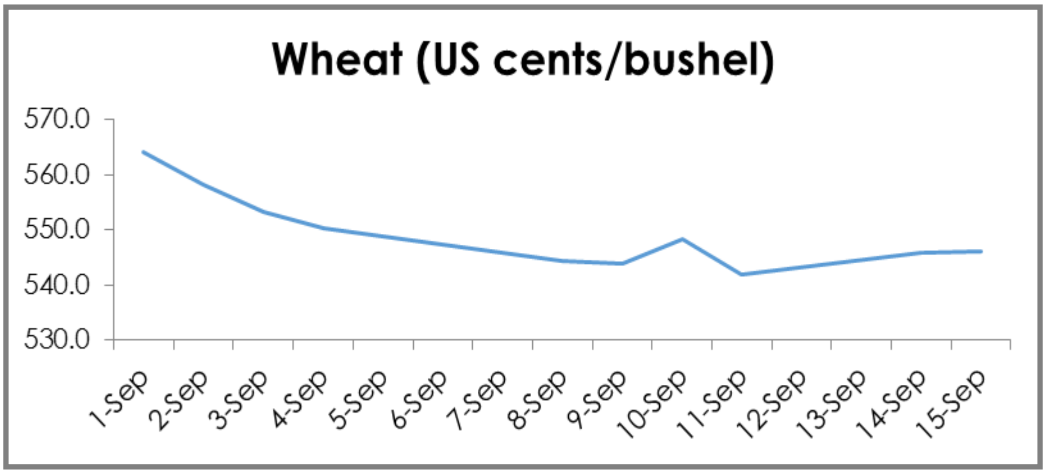
Cocoa is one of Nigeria's leading non-oil export commodity. Thus, a decrease in cocoa prices would result to lower export earnings and revenue for the government.

[22]EIU
[23]Bloomberg

Commodities Market– Imports

Wheat

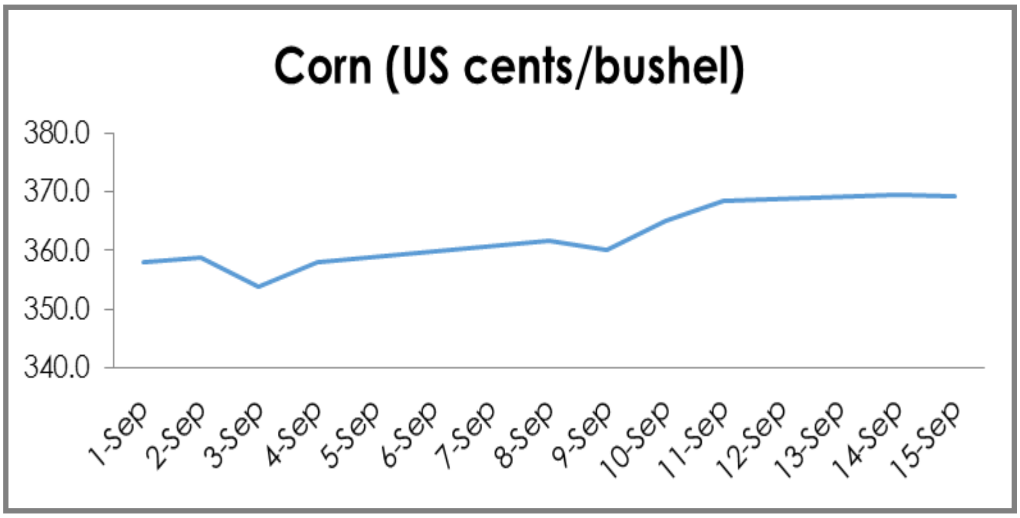
On the average, the price of wheat stood at $549.60/bushel during the review period, up 8.70% from $505.63/bushel recorded in the first half of August. The uptick in price was supported by strong demand from China for US wheat.



[24]

Corn

The price of corn averaged $362.30/bushel during the review period, up 10.90% from $326.70/bushel in the corresponding period of August. The increase in price was partly attributed to a robust demand from China amid supply shortages.



[25]

[24]Bloomberg
[25]Bloomberg

Outlook - Grains

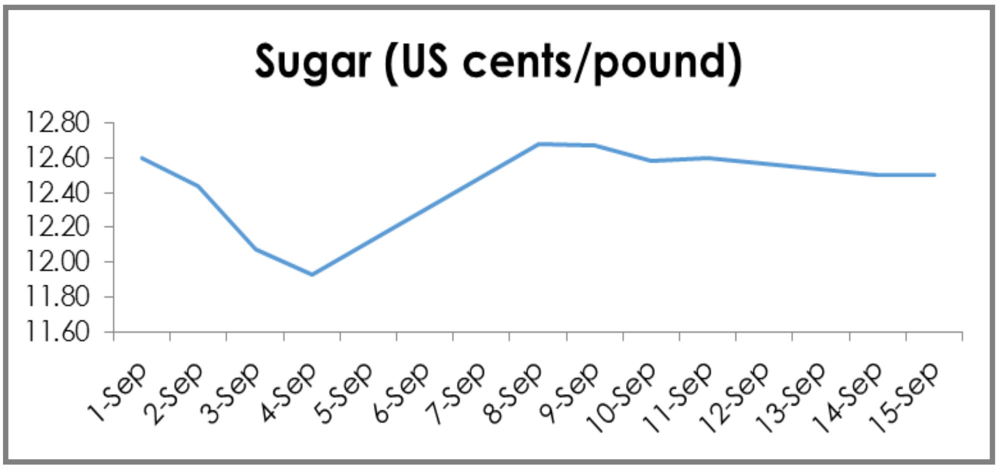
We expect grain prices to maintain the bullish trend in the near term on the back of supply concerns due to expectations of a decline in US crop yields.

Impact

An increase in the global price of grains will increase the production cost for domestic companies that are dependent on the importation of grains.

Sugar

During the review period, the average price of sugar declined by 2.66% to $12.46/pound from $12.80/pound recorded in the first half of August. The fall in price was as a result of ample sugar supply particularly from Brazil.



[26]

Outlook

Prices are likely to decrease further in the near term owing to surplus sugar production in Brazil.

Impact

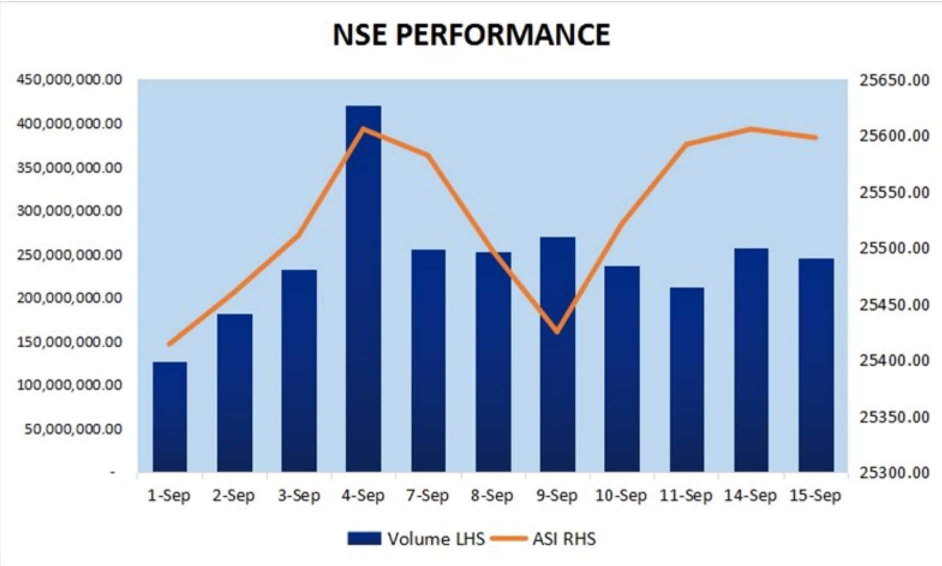
A fall in the global price of sugar will result in reduced input costs of sugar-producing companies in Nigeria.

[26]Bloomberg

Stock Market Review

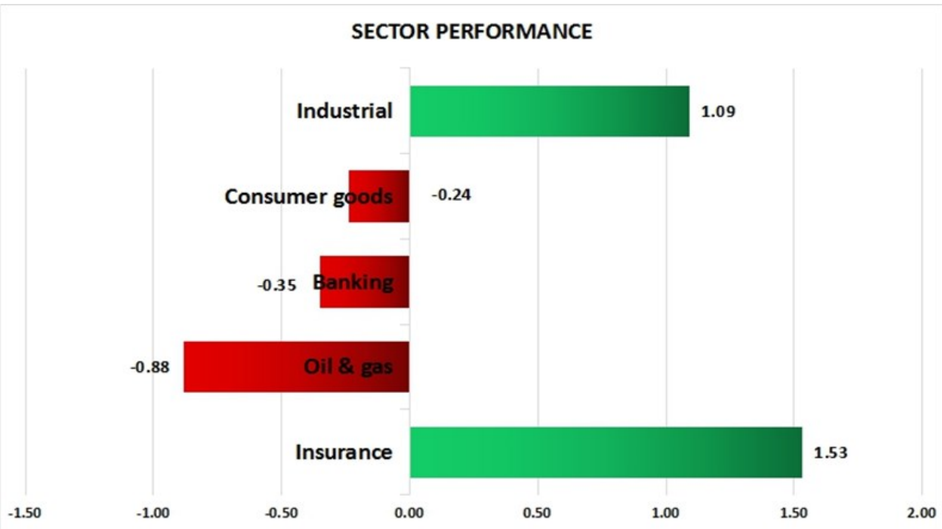
The Nigerian stock market closed on a positive note in the first half of September as it gained 1.07%to close at 25,597.96 points on September15th from 25,327.13 points on August 31st. In the same vein, market capitalization was up 1.06% (N140bn) to N13.35trn relative to its close of N13.21trn on August 31st. Meanwhile, the market has lost 4.63% YTD so far in 2020. In the 11 trading days of the review period, the market gained in 7 days and lost in four.

The NSE traded at a price to earnings (P/E) ratio of 9.01x as of September 15th, 1.24% higher than the close of August31st (8.90x). The market breadth was positive at 1.03x as 35 stocks gained, 34 lost while 94 stocks remained unchanged.



[27]

On the other hand, market activity level was positive in the review period. The average volume traded was up 15.74% to 244.42mn units in the second half of September from 211.18mn units in the second half of August. Similarly, the average value of trades increased by 26.23% to N2.31bn from N1.83bn in the review period.



[28]

[27]NSE and FDC Think tank
[28]NSE and FDC Think tank

The sector indices were mixed during the review period. The insurance and industrial sectors gained 1.53% and 1.09% respectively. The oil & gas sector lost the most (0.88%) followed by banking sector (0.35%) and consumer goods sector (0.24%).

Eterna Plc topped the gainers' list with a 41.05% increase in its share price. This was followed by Cornerstone Insurance Plc (17.86%), Wapco Assurance Plc (12.97%), UACN Property Development Co Plc (11.76%) and Lawunion and Rock Insurance Plc (11.65%).

TOP 5 GAINERS				
Company	**Aug-31 (N)**	**Sep-15 (N)**	**Absolute Change**	**Change (%)**
Eterna Plc	1.90	2.68	0.78	41.05
Cornerstone Insurance Plc	0.56	0.66	0.10	17.86
Wapco Assurance Plc	11.95	13.50	1.55	12.97
UACN Property Development Co Plc	0.85	0.95	0.10	11.76
Lawunion and Rock Insurance Plc	1.03	1.15	0.12	11.65

The laggards were led by Lasaco Assurance Plc (-19.35%), Initiates Plc (18.57%), International Breweries Plc (-13.51%), Tripple Gee and Co Plc (-12%) and Ardova Plc (-9.92%).

TOP 5 LOSERS				
Company	**Aug-31 (N)**	**Sep-15 (N)**	**Absolute Change**	**Change (%)**
Lasaco Assurance Plc	**0.31**	**0.25**	**0.06**	**-19.35**
Initiates Plc	**0.7**	**0.57**	**0.13**	**-18.57**
International Breweries Plc	**3.7**	**3.2**	**0.5**	**-13.51**
Tripple Gee and Co Plc	**0.5**	**0.44**	**0.06**	**-12**
Ardova Plc	**12.6**	**11.35**	**1.25**	**-9.92**

Outlook

We expect that the positive performance of the market will be short-lived. The increase in the inflation rate to 13.22% in August may force the CBN to adopt a contractionary policy stance. This will lead to higher interest rates and lead to lower stock prices.

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Corporate Focus:
Nigerian Breweries Plc

Market Capitalization: N382.65bn

Current Price: N47.85

Industry: Food, beverage and tobacco

Analyst's note

The Nigerian food, beverage and tobacco (FBT) industry was one of the industries badly affected by the lockdown and disruption to logistics and distribution. The industry contracted by 3.01% in Q2 from a 1.1% and 1.22% positive growth in Q1'20 and Q2'19 respectively. The breweries industry, a sub of FBT, is heavily dependent on income levels, exchange rate adjustments. It has been affected by lower consumer disposable income and a weaker currency that has led to higher import costs. The interstate lockdown in Q2'20 also affected supply chains, especially with the key sales markets (bars and restaurants) closed as part of the government's restriction measures. These have led to a plunge in brewers' sales revenue. With operating costs remaining high and sticky downwards, profit margins of companies in the FBT industry have thinned significantly.

Recent policy reforms have also impacted on the performance of brewers in Nigeria, however positively. For instance, the CBN's approval of only four companies to import 262,000 tons of maize, following its earlier complete ban will boost supply of the commodity. Sorghum, a substitute of maize, also used in brewing will experience a decline in its price due to the cross elasticity of demand; an increase in supply of maize will lead to reduced demand for sorghum and lead to lower prices of the latter. Also, the Federal Government's automation of the customs' process is expected to erase redundancies and reduce bureaucratic and inefficient processes. This is expected to lead to improved collection and faster turnaround time for importers such as those in the FBT industry. This will impact positively on productivity gains and output levels.

With the relaxation of the lockdown and gradual pickup in economic activity, we expect the breweries industry to recover albeit marginally. However with disposable income constrained and inflation stoking factors on the increase (higher electricity tariff hike and petrol prices), the demand for luxury items such as beverages will remain suboptimal. Nigeria's food inflation spiked to 16% from 15.48% and this trend is expected to continue.

COVID disruptions weigh on performance

The company reported negative performance along most line items. Its revenue declined by 10.8% to N151.81 billion in H1'20 from N170.19bn in the previous period, in line with industry trend. This decline was driven primarily by lower sales volume growth due to the lockdown and dwindling disposable income compounded by limited scope of price increase as competition stiffened.

The operating performance was reflective of the cost implication of supply chain challenges during the lockdown as return from operating activities declined by 38.5% to N15.05bn from N24.46bn in the same period in 2019. The company reported an increase of 29.9% increase in finance cost to N6.7bn from N5.1bn. The increase in finance cost can be attributed to the increase in borrowings during the period, it reported a 570% increase in borrowings to N112.7bn from N16.83bn as at end of the year in 2019.

Although margins also contracted, it shows more resilience which reflects management's attempt to manage costs. The company's gross margin declined to 39% from 42%, operating margin declined to 10% from 14% while net profit margin declined to 4% from 8%.

Recently, Heineken Brouwerijen B.V, the major shareholder of the company increased its holding to 37.9%. This could imply a possible capital raise or that the major shareholders are strengthening their existing position. We believe that this will also be beneficial to its current net-liability balance sheet exposure, hence dampening the adverse impact of a naira devaluation.

Industry and company overview

The Nigerian brewery industry dates to the pre-independence era when beer from assorted brands was imported into the country before World War II. Nigerians acquired a taste for continental European beer, leading to a significant increase in the quantity of imported beer during and after the war. This created an opportunity for a brewery to be set up in Nigeria.

The local brewery industry is the largest subsector of the food, beverage and tobacco sector in Nigeria, and the second-largest beer market in Africa. It has evolved over the years from a duopoly, with two firms sharing the market, to an oligopolistic[29] market structure with a strong multinational presence. The Nigerian brewery sector has also evolved from solely bottling activities to a diversified industry involved in the production of canned drinks (non-glass bottled drinks).

Nigerian Breweries Plc was incorporated in November 1946 as Nigerian Breweries Ltd and was converted to a public limited company in 1990. It started trading on the Nigerian Stock Exchange (NSE) on September 5, 1960. Heineken NV, one of the largest brewing companies in the world, currently owns a majority shareholding (55.19%) in Nigerian Breweries. Its primary business activities involve the brewing, marketing, and selling of alcoholic and non-alcoholic beverages (lager, stout, non-alcoholic malt drinks and soft drinks).

Nigerian Breweries is Nigeria's largest brewing company, accounting for over two-thirds of the brewery industry's market. The company pioneered brewing in Nigeria, starting with its first bottle of STAR lager brewed in June 1949 from its premier brewery, Lagos Brewery. Over the years, it has undergone several development processes to improve efficiency.

The company has since evolved rapidly across the country through the construction of new breweries and the acquisition of existing ones. Ever since its commissioning in 2003, the Ama Brewery (Enugu state) maintained its position as the biggest and most modern brewery in Nigeria. The company also acquired majority shares in Sona Systems Associates Business Management Ltd and Life Breweries Company Ltd in 2011. Following its merger with Consolidated Breweries Plc in 2014, it bought Imagbon (Ogun state), Awo-Omamma (Imo state) and Makurdi Breweries.

[29]A state of limited completion in which a small number of brewing multinationals battle for position in the Nigerian beer market space

The company also has a rich portfolio of high-quality alcoholic and non-alcoholic products, popular in Nigeria. It has a wide range of brands that cater to the needs of different segments of the market. These include Heineken, Star, Gulder, "33" Export, Goldberg, Legend Extra Stout, Maltina, Amstel Malt, Hi-malt, Star Radler and Star Lite. Most of its brands are leaders in their segmented markets. Nigerian Breweries has a growing export business that dates to 1986. While the domestic market remains the dominant market for these brands, some of the products are exported to over 13 countries across the UK, South Africa, West Africa, Middle East, and the US.

Other leading players in the brewery industry include Guinness Nigeria (a subsidiary of Diageo) and International Breweries (a subsidiary of ABInBev).

International Breweries is the biggest threat to Nigerian Breweries. International Breweries' cheap pricing strategy, strong mainstream products (Trophy and Hero, enable it to gain market presence in major regions in the country.[30] Although NB may lose some market share, it will remain a market leader in the brewing industry.

[30] FSDH

Management

Capable of capitalizing on potential growth opportunities in the food industry

Mr. Jordi Borrut Bel has served as the Managing Director and Chief Executive Officer of Nigerian Breweries since January 22, 2018. His career started with Heineken, Spain, in 1997 as the sales representative/wholesale manager. He has since gained over 20 years of experience in the brewing industry across France, Slovakia and the Netherlands. He successfully led the company through turbulent periods by strengthening the company's route-to-market and launching successful innovations. He is also a board member of Bralirwa Ltd, a subsidiary of Heineken in Rwanda.

Chief Kolawole B. Jamodu has been the chairman of the board of directors, since January 1, 2008. He was appointed to the board as a non-executive director in 2006. Chief Kolawole is a chartered accountant, an industrialist, and a former minister of industry of the federal government of Nigeria. He previously worked as the chairman and group chief executive of the PZ Group. He has also led organizations such as Universal Trust Bank Plc, Manufacturers' Association of Nigeria, and United Bank for Africa Plc. He has served as part of the national economic management team under former president, Goodluck Jonathan.

MD/CEO

Mr. Jordi Borrut Bel

Chairman

Chief Kolawole B. Jamodu

What the bulls and bears say

Bulls say

- Large market size and market leadership
- Continuous product innovation
- Rich product portfolio for both alcoholic and non-alcoholic drinks
- Portfolio of leading brands
- Strong and effective channels to the market

Bears say:

- Stiff competition
- Shift of market preference to low-priced products
- Congestion at the port
- Unfriendly business environment

Risk and outlook

The major risks that could prevent Nigerian Breweries from achieving its goals of boosting earnings, increasing sales and managing costs are its exposure to credit, liquidity, and market risk (currency and interest rate) arising from financial instruments as well as persistent macroeconomic challenges. The board established the risk management committee to develop and monitor the company's risk management policies in co-operation with its internal audit.

In managing foreign currency risk, the company participates in financial instruments provided by the central bank of Nigeria including forward contracts and futures.

In managing interest rate risk, the company aims to reduce the impact of short term fluctuations on earnings by opting for a mix of fixed and variable interest rates in its financing operations, coupled with the use of other financial instruments such as commercial paper.

The security challenges that have affected the company's sales in the northern part of the country may continue to have a negative impact on growth projections and market penetration. The company mitigates capital risks by maintaining an efficient capital structure through adjusting its debt to equity ratio.

The shift of consumers to value products instead of premium brand products poses a threat to Nigerian Breweries' sales prospects. The risks facing Nigerian Breweries could limit the achievement of its long term objectives.

Economic Outlook

Nigeria's oil production inched up to 1.482mbpd in August above the OPEC quota of 1.4mbpd. This is likely to receive pushback from the oil cartel and force the country to reduce oil production in the coming months. Lower oil production coupled with the dwindling global Brent price could depress government revenue and external reserves further.

The good news is that the gradual reopening of the economy could boost activities in the manufacturing sector and push PMI above 53pts in September. However, this may have a negligible effect on Q3 GDP, which is expected to remain in the negative territory. Inflationary pressures are also likely to heighten in the coming month following the hike in PMS price and commencement of cost reflective electricity tariffs. These cost-push factors could result in an increase in Nigeria's headline inflation to 13.5%-13.7% by September-end. We also expect the exchange rate to remain volatile in the near term owing to increased demand from students, travelers and medical tourists.