FDC

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PRISM

BIZNOMICS

CONTENTS

The Prism Overview:
Global & Domestic

The global economic landscape is in flux, marked by surging oil prices, elevated interest rates and the lingering Russian-Ukraine war. While the war has attracted Western sanctions against Russia, the recent decision by Russia to ban the export of diesel and petrol is raising concerns that it may be a retaliatory measure in response to these sanctions. However, Russia's primary objective in implementing this ban is to stabilize domestic oil prices and enhance the country's fuel supply. Nonetheless, Russia's export ban has led to a further increase in global oil prices. Russia is one of the world's largest suppliers of diesel and a leading producer of crude.

Currently, global oil prices are hovering around $92-95pb after peaking at $95.47pb on September 19, the highest since November 2022 due to the voluntary cuts by Russia and Saudi Arabia. The countries agreed to extend their oil supply cuts (totalling 1.3mbpd) till the end of the year.

Higher energy costs continue to fuel global inflation, increasing the chances of further rate hikes by global central banks. The US Fed, at its last meeting, paused (5.25%-5.5%) on increasing rates but signalled one more rate increase before year-end. The European Central Bank (ECB) also hiked interest rate by 0.25% to a record high of 4.5%p.a. on September 14.

Higher interest rates have ushered in a new normal of expensive borrowing costs from commercial banks and choppy investment inflows into emerging and frontier economies like Nigeria. As of Q1'23, capital inflows into Nigeria fell by 28% to $1.13bn from $1.57bn in Q1'22. The global perspective in this Prism provides a deep-dive on how higher interest rates are reshaping the global banking landscape.

Meanwhile, Nigeria is awash with a myriad of macroeconomic challenges. The FTSE Russell downgraded the Nigerian Stock Exchange (NGX) from its "Frontline" status to "Unclassified Market", triggering sell-offs on the NGX and, resulting in a loss of N757 billion in two days. Though the stock market recovered modestly afterwards due to heightened domestic investor interests in banking stocks, concerns about Nigeria's forex supply hassle are beginning to gain ground. The naira, plunged by 25% YTD to a new low of N993 at the black market.

The economic articles in this report unpack strategies for the government to boost forex supply, including resource diversification and seizing opportunities presented by AfCFTA (if fully implemented). There's also a corporate focus on the third-largest brewery company in Nigeria— Guinness and an insightful outlook for the next month.

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AFCFTA:
The Path to Full Implementation

The African Continental Free Trade Area (AfCFTA) is the world's largest free trade area with a single market of about 1.3 billion people and a combined GDP of $3.4 trillion. The AfCFTA aims to eliminate trade barriers and foster intra-African trade.

About 84% of the 55 African countries have ratified the trade agreement and deposited their instrument of ratification with the African Union Commission. AfCFTA is expected to boost economic growth in member states as they specialize in areas of comparative advantage. Also, the large market will aid foreign direct investment, creating jobs for Africans. Unemployment in sub-Saharan Africa is 6.7%, 0.9% above the global average (5.8%).

While the benefits of AfCFTA are enormous, there are two main barriers to AfCFTA's full implementation in Africa. One barrier is the lack of political will and the unwillingness of the individual member states and their governments to successfully implement AfCFTA. The second factor is the prevalence of non-tariff barriers, particularly poor facilitation of cross-border goods, a lack of transparency in currency markets, and

> "About 84% of the 55 African countries have ratified the trade agreement and deposited their instrument of ratification….

ineffective support for small and medium enterprises (SMEs).

Policymakers across the African continent have been reluctant to eliminate trade tariffs in line with the initiative. They are concerned that the elimination of trade tariffs could lead to a loss of revenue for the government, especially at a time when public finance in most African countries is struggling. However, intra-African tariffs account for a minimal portion of African tariff revenue.

In 2015, intra-African trade tariff revenue amounted to only 0.1% of African GDP ($3.5 billion)[1] compared to its tariff on imports from the rest of the world, which is about 1.5% ($37 billion) of African GDP. The benefits that accompany intra-African trade liberalization – high GDP growth, increased investment (private and foreign) and high employment – outweigh the losses from the elimination of intra-African trade tariffs[2]. Governments can benefit from increased revenue generated from higher tax collection as the economy grows and employment increases. The World Bank estimates a 3% growth in government tax revenue at the continental level due to higher economic activities induced by implementing of AfCFTA[3].

For non-tariff barriers, African economies with extremely poor infrastructure such as road infrastructure, energy, technology, ports, etc. are likely to incur increased trade costs and low productivity, making the economy less competitive amongst other African economies. For instance, government policies like restrictions on foreign exchange could lead to high currency convertibility risks for foreign investors and discourage international trade. Also, bureaucratic bottlenecks such as excessive and complex administrative requirements related to trade, licensing and regulatory burdens, and inefficient port and border operations can hinder the prosperity of AfCFTA in member countries.

The path to a successful implementation of AfCFTA involves identifying and eliminating the non-tariff barriers to trade, and introducing policies to support small-scale businesses (SMEs) and sectors that could negatively be impacted by the implementation of AfCFTA through increased competition.

Eliminating non-tariff barriers to trade

Non-tariff barriers have a significant impact on reducing and restricting trade compared to tariff barriers[4]. Eliminating non-tariff barriers to trade is estimated to produce a gain of $20 billion annually[5]. Therefore, policymakers must seek to significantly reduce non-tariff barriers to trade by spending more on infrastructure development, simplifying and reducing administrative processes, especially

1 Dr. Jonathan D. Moyer, Dr Abigail Kabandula, David K. Bohi, Taylor Hanna, Dr Ibrahim Mayaki, & Martin Bwalya. 2020. "Conditions for Success in the Implementation of the African Continental Free Trade Agreement". Frederick S. Pardee Center for International Futures and The AfricanUnion Development Agency-NEPAD. https://au.int/sites/default/files/documents/38076-doc-afcftaenglishfinal20200123-2.pdf.

2 Dr. Jonathan D. Moyer, Dr Abigail Kabandula, David K. Bohi, Taylor Hanna, Dr Ibrahim Mayaki, & Martin Bwalya. 2020. "Conditions for Success in the Implementation of the African Continental Free Trade Agreement". Frederick

3 Maryla Maliszewska. 2020. "The African Continental Free Trade Area: Economic and Distributional Effects". World Bank Group. https://www.wto.org/english/thewto_e/acc_e/afcfta_feb11maryla.pdf

4 Institute for Government. 2017. "Non-tariff barriers". IGF Academy.https://www.instituteforgovernment.org.uk/article/explainer/non-tariff-barriers#:~:text=A%202009%20study%20of%20the overall%20market%20access%20trade%20restrictiveness.

5 UNCTAD.2013." Trade and Development Report".United Nations Publications.https://unctad.org/system/files/official-document/tdr2013_en.pdf.

in relation to trade, and promoting an efficient foreign exchange market for the facilitation of trade payments and easy repatriation of profits by foreign investors.

Facilitating an efficient foreign exchange market involves several critical components: complete transparency in currency pricing and trading volume information, alignment of exchange rates with prevailing economic fundamentals and market sentiments (accurate price discovery), minimizing transaction costs associated with currency trading, and mitigating arbitrage opportunities. This will boost investor confidence and enable member countries to benefit from AfCFTA.

A notable example is Singapore, which made substantial investments in modernizing and streamlining its customs procedures through the establishment of the National Single Window in 1989. The country has also made continuous upgrades and enhancements over the years to keep pace with technological advancements and changing trade requirements[6]. This digital platform allows businesses to electronically submit all trade-related documents, eliminating paperwork, expediting processing, and enhancing transparency.

Furthermore, Singapore has one of the busiest and most efficient ports in the world. The country has continuously invested in port and transportation infrastructure, which ensures that commodities flow quickly and easily throughout the country. Singapore's elimination of non-tariff trade barriers has boosted international trade and its competitiveness globally. International trade has significantly contributed to Singapore's economy. For instance, in 2022, its trade-to-GDP ratio stood at approximately 337%[7]. Some countries in Africa such as Kenya, Rwanda, Uganda and Tanzania have also adopted similar systems, leading to faster clearance and shipment of goods, increased competitiveness, and improved business environment.

South Africa is another success story, concerning its efficient foreign exchange market's role in facilitating international trade. According to the IMF, South Africa's financial markets are the most developed and liquid in Africa. Based on the Bank for International Settlements' triennial survey, South Africa's foreign currency market turnover has remained among the top 20 in the world[8]. This feat is primarily due to the transparency, low transaction costs, accessibility, and market integrity within South Africa's foreign exchange market, which facilitates its international trade payments and attracts foreign investments. International trade accounted for 56% of South Africa's total GDP as of 2021 compared to an average of 46% in sub-Saharan Africa[9].

Recognizing and developing the SMEs

AfCFTA is expected to spur

6 King, J. and Konsynski, B. (1990). Singapore TradeNet: A Tale of One City. Harvard Business School. https://hbsp.harvard.edu/product/191009-PDF-ENG
7 The World Bank.2022." Trade (% of GDP)".World Bank national accounts data, and OECD National Accounts data files. https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS?locations=SG
8 Jennifer Elliott, IMF and Eva Gutierrez, World Bank.2022." Financial Sector Assessment Program".IMF. https://www.imf.org/-/media/Files/Publications/CR/2022/English/1ZAFEA2022006.ashx
9 The World Bank.2021." Trade (% of GDP)".World Bank national accounts data, and OECD National Accounts data files.https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS?locations=SG

competition among African industries and firms. However, the viability of SMEs could be threatened as industries with large economies of scale benefit mostly from AfCFTA. Therefore, policymakers must recognize SMEs and formulate policies that will boost their growth. This involves increasing access to finance, capacity-building programs, technical assistance, and simplifying regulatory processes to enhance the competitiveness of SMEs and enable them to benefit from the opportunities that AfCFTA offers.

For example, the Chinese government implemented a series of policies and reforms to support SMEs, which include tax incentives, reduction in administrative burdens, as well as easier access to financing. The government recognized the importance of SMEs in fostering innovation, creating jobs, and promoting economic development. China also invested heavily in education and workforce development resulting in a skilled and educated workforce, which is crucial for the growth and success of SMEs. The development of SMEs in China contributed to economic growth and enhanced competitiveness in the global market. According to the Organization for Economic Co-operation and Development (OECD), SMEs contributed over 60% of total GDP, 50% of tax income, 79% of job creation and 68% of exports in 2020[10].

Conclusion

While the AfCFTA holds immense promise for Africa's economic development, overcoming challenges related to political will, non-tariff barriers and the growth of SMEs is essential for its successful implementation. By addressing these issues, African nations can unlock AfCFTA's full potential and usher in a new era of economic growth, job creation, and increased intra-African trade.

Local Commodities: Key to Nigeria's Green Economy

A green economy is a resource-efficient and socially inclusive economy that practices and encourages sustainable economic growth and development using environmental principles. Enhancing Nigeria's green economy would generate economic growth and foster development in lives while aiding ecological enhancements. Notably, the dominance of non-renewable resources, such as crude oil, constitutes approximately 79%[11] of Nigeria's exports in foreign trade. This statistic underscores Nigeria's over-dependence on oil, exposed vulnerability to global oil market fluctuations. Recent reductions in OPEC's oil production, driven by supply constraints, are set to affect the country's foreign revenue and reserves.

> Nigeria's heavy reliance on oil has resulted in several negative impacts on its green economy.

Oil vs Non-oil

Nigeria's heavy reliance on oil has resulted in several negative impacts on its green economy. Unlawful activities linked to oil smuggling, including spills, have precipitated environmental degradation. These oil spills have contaminated the waterways, causing harm to aquatic life and vegetation, and other detrimental health

10 OECD. 2022. "Financing SMEs and Entrepreneurs 2022". OECD iLibrary. https://www.oecd-ilibrary.org/sites/a3891ad8-en/index.html?itemId=/content/component/a3891ad8-en

11 Ndigwe, C. 2023. "Nigeria earned N5trn from oil sales in first quarter of 2023". Businessday NG. https://businessday.ng/energy/article/nigeria-earned-n5trn-from-oil-sales-in-first-quarter-of-2023/

risks for residents and communities. Oil production growth has also driven deforestation and destroyed habitats, threatening biodiversity. Its expansion has also resulted in the loss of arable land, adversely impacting agriculture and livelihoods. Competition and desire for oil and its resources have led to conflicts, most significantly in the Niger Delta region, resulting in social unrest and disparities in access to aid.

Alternate commodities would be beneficial in economic downturns like Nigeria's current situation. Increasing Nigeria's non-oil export commodities (agricultural, mineral, or other raw materials) would improve Nigeria's revenue. Such action would lessen the drastic effects of oil volatility and improve the country's green economy. Diversification would stimulate expertise, innovation and competitiveness[12] within the domestic market. Furthermore, implementing policies focused on bolstering local commodity exports and thoroughly investing their returns into low-cost renewable energy production could generate excellent economic yields for Nigeria and make progress towards safeguarding the country's future.

While the revised unemployment statistics in Nigeria may suggest that only 3 million out of the country's 72 million working-age population are officially jobless, the harsh reality reveals that a staggering 133 million individuals are grappling with multidimensional poverty, struggling to secure the adequate income to meet their basic needs.

Nonetheless, increasing local production of agricultural commodities would help mitigate unemployment by creating new jobs and increasing employment opportunities. Investing more significantly in locally produced commodities, such as cashews or salt, would boost the agricultural sector. Similarly, mineral resources like steel would stimulate the Nigerian economy as there would be fewer import leakages due to more locally sourced foods and products and greater money circulation within our economy. There would be fewer CO2 emissions, a significant contributor to climate change, as these agricultural resources would travel less distance to consumers.

12 Akintonde, O. 2023. "Council and German agency partner to boost commodity production, Voice of Nigeria".https://von.gov.ng/council-and-german-agency-partner-to-boost-commodity-production/

Additionally, renewable energy would increase employment across various sectors related to the renewable energy industry, such as manufacturing, operations and maintenance. This rise in jobs would improve livelihoods and stimulate Nigeria's local economy. Foreign direct investments would also increase as many foreign companies are keen on improving their environmental sustainability and would be attracted to Nigeria's commitment. These investments would bolster economic growth and contribute to infrastructure development. Similarly, integrating renewable energy would foster stable development while preserving the environment for future generations.

Most renewable energy sources either produce minimal or no global warming emissions[13]. This characteristic allows countries to decrease their use of carbon-intensive energy sources when transitioning to renewable sources. Investing in low-cost renewable energy would reduce Nigeria's use of fossil fuels while helping it mitigate the adverse effects of climate change and heighten its energy security. This increase in Nigeria's energy security would contribute to stabilizing energy prices as renewable sources are less susceptible to the price volatility commonly associated with fossil fuels[14]. Furthermore, improving its energy security would increase competition among energy suppliers and protect consumers from oil price spikes.

> Sweden's integration of eco-friendly practices with its steel production has boosted its economic growth and illustrated the possibility of co-existing environmental sustainability with steel production, making Sweden a frontrunner in low-carbon steel production.

Lessons from Sweden

Steel has played a pivotal role in Sweden's thriving green economy. Sweden, the world's top green economy, saw increased steel production rise during the global financial crisis in 2008. Since then, it has undergone technological advancements and adopted sustainable practices to reduce its carbon footprint. Most of Sweden's finished steel output is exported as its steel companies specialize within different aspects/specialties[15].

Sweden's integration of eco-friendly practices with its steel production has boosted its economic growth and illustrated the possibility of co-existing environmental sustainability with steel production, making Sweden a frontrunner in low-carbon steel production. According to the OECD, approximately 26.6% of workers are, on average, in Sweden's green economy. The United Nations COMTRADE database shows Sweden's iron and steel exports accounted for $8.8 billion in 2022. However, the steel industry accounts for 7-9% of the world's CO2 emissions[16], and Sweden is looking for ways to

13 Union of Concerned Scientists 207." Benefits of Renewable Energy Use. Union of Concerned Scientists. https://www.ucsusa.org/resources/benefits-renewable-energy-use"
14 Roosevelt Institute. 2022. "Energy Price Stability: The Peril of Fossil Fuels and the Promise of Renewables."https://rooseveltinstitute.org/publications/energy-price-stability/.
15 2023. "Industry Facts and Statistics Jernkontoret".https://www.jernkontoret.se/en/the-steel-industry/industry-facts-and-statistics/deliveries-and-steel-consumption/
16 Liljas, P. 2022. "The green revolution sweeping Sweden", The Washington Post. https://www.washingtonpost.com/climate-solutions/interactive/2022/sweden-green-revolution-steel-climate-change/

make its production greener.

Embracing low-carbon steel production needs substantial research and development within Nigeria's steel industry, requiring Nigeria to embrace technological advancements by fostering collaboration between research institutions, academia and industries. Such technological evolution would position Nigeria as a hub for pioneering sustainable industrial practices.

Nigeria can emulate Sweden's low-carbon steel production by setting specific goals and heavily allocating resources to research and development to adopt innovative technology. There would also be a need to establish a system to invest revenues generated through low-carbon steel exports into projects such as reforestation that promote ecosystem health. Governments can incentivize companies to adopt greener policies and cleaner technologies through stringent regulations. Additionally, encouraging sustainable farming practices would help Nigeria promote better water management, especially in rural areas, minimize harmful chemical use, and reduce land degradation.

Embracing and harnessing the potential of Nigeria's locally produced or found commodities can significantly contribute to Nigeria's green economy. Nigeria can transition towards a future characterized by enhanced economic well-being and heightened environmental awareness. This transition would require a fundamental stride towards securing a sustainable nation across generations and governments looking at long-run benefits rather than short-term gains. Nigerian governments must create a conducive policy environment that incentivizes investments and encourages research and development.

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Global Perspective: Higher interest rates signal the end of one-stop-shop banks

In early February, the St Louis branch of the Federal Reserve published a blog post warning that higher interest rates could "complicate" banks' finances. The post was as prescient as it was optimistic. The Fed's supervisors said rising interest rates created both "challenges and opportunities for banks". They suggested that banks should carefully analyse the situation, but also said there were several steps banks could take to mitigate any issues. Less than a month later, Silicon Valley Bank (SVB) failed, largely due to the effect of sharply higher interest rates, kicking off the worst period of banking turmoil since the Great Financial Crisis. Signature Bank quickly followed into the abyss. Shares of dozens of banks plunged in value, raising questions about their survival, too.

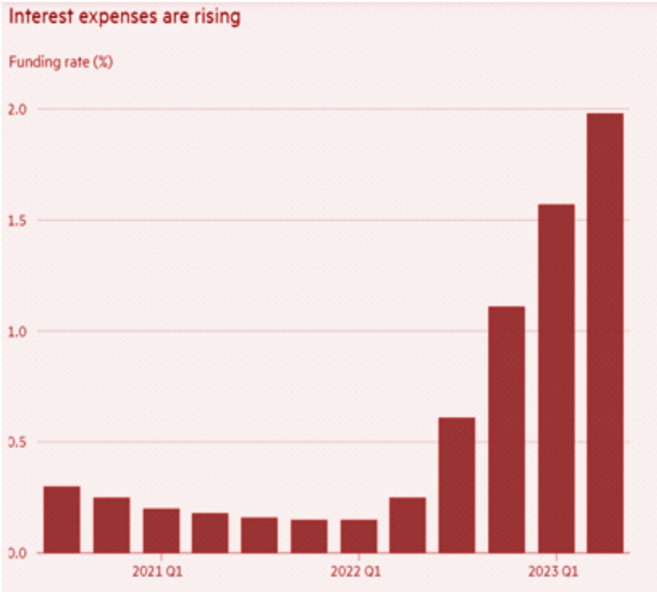
In Europe, UBS bought the long-suffering Credit Suisse in a government-backed deal that saved its rival from collapse. Emergency measures from the Federal Reserve, billions of dollars from

> Big lenders are starting to retreat, and in some cases exit, from consumer banking, as income becomes squeezed.

the federal deposit insurance fund, and tens of billions of loans from the government-backed Federal Home Loan Banks quelled the crisis. Few, if any, banks now seem at risk of failing. However, while the crisis has passed, the challenge from higher interest rates, as the St. Louis Fed warned in May, has not. Higher interest rates have ushered in a new normal in the banking industry. A slowing economy and higher scrutiny from regulators following recent bank failures have largely capped the amount of lending that banks are able to do at elevated rates. And banks are seeing the effects of higher rates on borrowers, particularly those in commercial real estate. Defaults on corporate loans, which generally carry interest rates that float — meaning they automatically adjust with market rates, not just when the borrower refinances — are also on the rise.

The European Central Bank warned in May that European lenders, such as SVB and other US banks that ran into trouble, would see the value of their assets fall faster, on average than the value of their debts — a particularly bad scenario for a bank if interest rates continued to rise. For the average bank, the central bank concluded, the drop in book value would be a very manageable 4 per cent. But the ECB also found that, for a quarter of European banks, the hit from rising interest rates would be high enough to force those banks to take steps to mitigate the damage. Already, a number of institutions, including Citigroup and Goldman Sachs, appear to be abandoning the notion that the best model for a global bank is to offer all services to everyone — the supermarket model of banking — something that seemed to be banking gospel just a decade ago. “You have to look at each business from the ground up and not bottom down at this point,” says Greg Hertrich, who is the head of deposit strategy at Nomura. “Twenty-five years ago, everyone wanted to be a one-stop shop, and that has changed.”

The biggest effect of rising rates, at least so far, has been on the banks’ bottom lines. For much of the past decade, banks have been one of the biggest beneficiaries of low interest rates, and essentially — at least for them — free money. With interest rates near zero, depositors had nowhere else to go with money that they did not want to risk in the market. As a result, customers had to accept — and eventually got used to — receiving no interest on their accounts. The rise of Internet banking, along with ATM and other account fees, made bringing in customers and their deposits all the more lucrative for banks. That started to change in early 2022 when the US Federal Reserve began raising interest rates to slow quickly rising inflation. In the first quarter of last year, the average US bank had an annual-equivalent funding rate — that is how much in interest it paid compared with its total assets — of 0.15 per cent. That funding rate has jumped nearly 12 times to just under 2 per cent in the past 18 months, mostly driven by the rising costs of deposits, with some banks offering interest rates on accounts in the 5 per cent range. Lending income is rising as well, but not nearly that fast.



In the second quarter of 2023, the average bank saw its interest income rise just 8 per cent from the quarter before. Interest expense, however, jumped 27 per cent. "It is the fact that funding costs have gone up and your assets, your loans and bond investments are worth less," says Hertrich. "My guess is that they are going to pull every lever that they can." Some banks are already starting to retreat from, or even exit, consumer banking. Bank of America chief executive Brian Moynihan had long talked about the importance of bank branches. But even BoA is cutting branches at a time when the cost of bringing in new deposits and holding on to the ones you have, is much greater than it has been for some time. Last year, the number of BofA branches fell to 3,900, down 7 per cent from the year before. It was the first time the bank had fewer than 4,000 branches since shortly after its merger with NationsBank in the late 1990s.

Just a year ago, Goldman Sachs was investing heavily in consumer banking in the UK, in an effort to win customers for its fledgling online bank Marcus. These days, it appears to have lost its interest in Marcus and consumer banking in general, both in the UK and at home in the US. Late last year, Goldman stopped making consumer loans through Marcus and scrapped plans for a checking account. It did recently launch a high-interest savings account, initially paying close to 4.5 per cent a year, but in a partnership with Apple and under the iPhone maker's brand, not Marcus. Emmanuel Dooseman, global head of banking at accounting and consulting firm Mazars, says there are only so many options for banks. Many lenders, he points out, committed to long-term loans when interest rates were still low, which will weigh heavily on profits. There could, he says, be a renewed interest in small business lending, as well as mortgage lending, where rates have risen. But that will expose banks to the risk that high-interest loans made now will go unpaid if the economy sours. "There is no short-term answer," notes Dooseman. The only way for banks to deal with lower lending income is to cut costs until profitability rebounds. Last week, Truist, one of the US's largest banks, announced a fresh round of cuts that it says will save $750mn dollars in expenses per year. "There are no quick fixes," says Dooseman. "It's just time."

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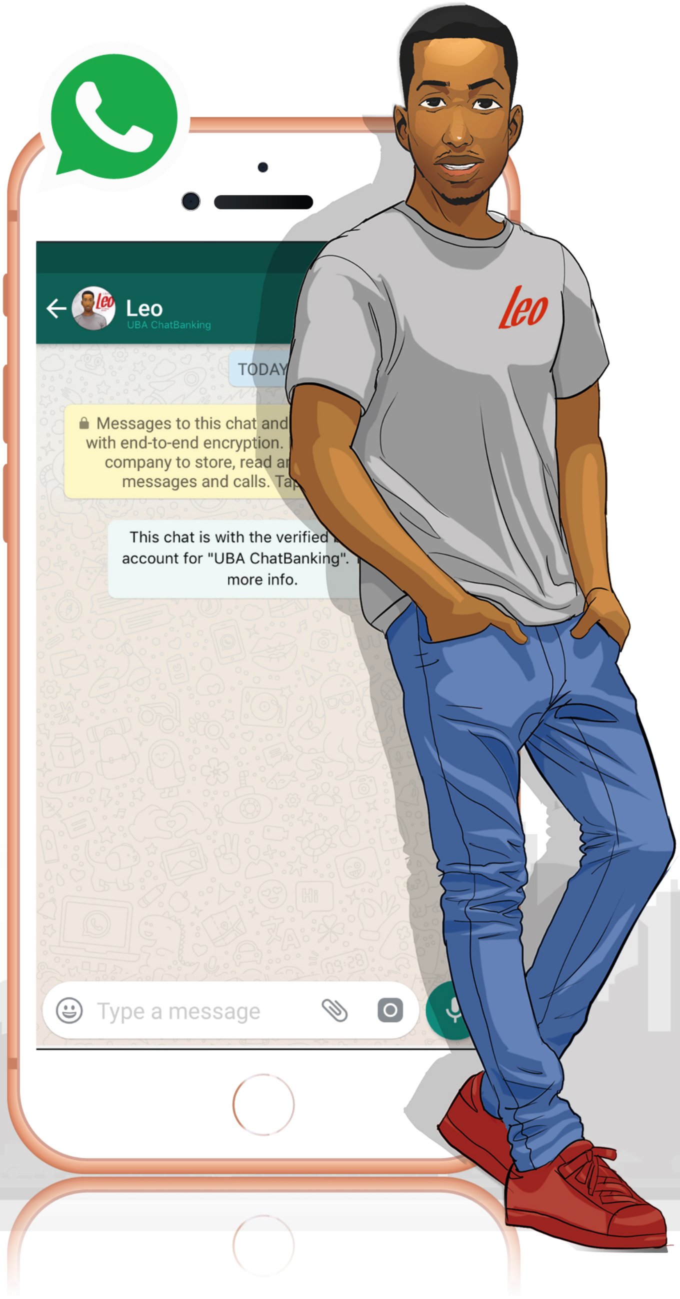

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Corporate Focus

Market Cap.	N142.37 billion
Share Price	N65 per share
Industry	Food, Beverage & Tobacco

Company Overview

Guinness Nigeria Plc, a Nigerian-based subsidiary of Diageo Plc, is one of the largest breweries in Nigeria. Incorporated in 1950 as a trading company importing Guinness Stout from Dublin, Guinness Nigeria was eventually listed on the Nigerian Stock Exchange in 1965.

Since then, the company has evolved into manufacturing, brewing, packaging, marketing, and selling alcoholic beverages such as Guinness Foreign Extra Stout, Guinness Extra Smooth, Herbs Lite, Snapp, Master's Choice, Orijin Spirit Mixed Drink, and Orijin Bitters. In 2018, Guinness Nigeria Plc began polyethylene terephthalate (PET) production lines for some of its products (Malta Guinness, Orijin Zero, and Dubic Malt).

In addition to acquiring the rights to import, market, distribute, and sell in Nigeria, the company also acquired the right to locally manufacture some of Diageo's mainstream brands. Hence, Guinness has successfully catered to different consumer segments in Nigeria. Some of the company's other popular brands include Harp, Guinness, Johnnie Walker, Baileys, Smirnoff, and Gordon's Dry Gin.

ANALYST NOTE

Guinness Nigeria Plc released its 2023 full-year results for the period ended June 2023, showing it reported a loss after tax of N18 billion compared to a N15.6 billion profit in 2022 after its finance costs soared due to the naira's devaluation. The last time Guinness reported a loss this profound was during the COVID-19 pandemic in 2020, when it reported a loss after tax of N12.5 billion. Unlike in 2020, when the loss was attributed to COVID-19, Guinness was faced with hydra-headed challenges this time. Nonetheless, the company defied all odds and declared dividends ostensibly out of retained earnings.

Impressive increase in topline revenue

Guinness, a long-standing player in the Nigerian beverage and alcohol industry, had a positive top-line performance despite facing severe macroeconomic challenges such as rising inflation, currency devaluation, temporary cash scarcity, and insecurity. In the financial year ended June 30, 2023, the company's turnover increased by 11% to N229.44 billion compared to N206.82 billion in the corresponding period in 2022. The rise in the company's turnover was due to an uptick in its sales in Nigeria, which accounts for over 99% of the company's revenue. Domestic sales rose by 11% to N227.3 billion, compared to export sales, which increased by 7% to N2.09 billion. The revenue growth stemmed from strategic pricing, successfully deploying the product mix across categories to counter cost inflation, an optimized route-to-consumer approach that improved outlet coverage, and the use of its B2B platform to improve distribution efficiency.

Uptick in cost of sales and operating expenses dampens margins

The foremost brewery's cost of sales increased by 12.7% to N151 billion from N134 billion in 2022. Meanwhile, gross profit was up 7.5% to N78.13 billion compared to N72.66 billion in 2022 due to revenue growth. Guinness' administrative expenses grew over 2x ahead of sales revenue to N16.97 billion at the end of the financial year. This, coupled with the 10.4% increase in marketing and distribution expenses to N41.23 billion, resulted in a 13% uptick in operating costs to N58.3 billion. Despite the rise in costs, Guinness still managed to generate an operational profit of N23.36 billion, 2.3% lower than N23.9 billion in 2022. This exerted downward pressure on the company's operating margin, which declined to 10.18% from 11.55% in 2022.

Weak bottom line performance triggered by exchange rate losses

In FY'23, Guinness reported a whopping net finance cost of N45.49 billion, wiping off the entire operating profit of N23 billion it had generated. This was despite its tax credit of N3.97 billion. Guinness' net finance cost surged by over 20,000% from N225 million to N45 billion in FY'23. The increase in net finance costs stemmed from the 2,400% increase in finance costs to N53.28 billion from N2.13 billion in FY'22, offseting the 300% rise in finance income to N7.78 billion. The spike in finance costs was a result of the intense volatility of the naira and the unavailability of forex at the official foreign exchange window. In Q2'23, the Central Bank of Nigeria (CBN) floated all the exchange rate windows, causing the devaluation of the naira from N419/$ to N760/$. Compared to its unrealized exchange rate gain of N5.5 billion, this led to a massive unrealized forex loss of N46 billion, up from N222 million in 2022. Consequently, Guinness Nigeria ended the year with a loss of N18.2 billion as against a profit of N15.6 billion in 2022, its first full-year loss since 2020.

Industry Overview

The breweries industry is a subset of the food, beverage, and tobacco (FBT) industry, which is under the manufacturing sector and a major employer of labor. In 2020, the brewery industry was adversely affected by the global economic downturn, lockdown, and disruption induced by the pandemic. Since then, the lingering weak macroeconomic environment, pressuring consumers' disposable income and tough business environment has weighed negatively on the performance of the FBT industry.

Additionally, the forex illiquidity and weaker naira have increased the cost of production for breweries, which have a high import content. However, the breweries industry is expected to deliver great value in the medium to long term on the back of Nigeria's growing population and favorable demographics, low consumption per capita, and increasing opportunities for exports under the African Continental Free Trade Area Agreement (AfCFTA). There is limited room for pricing, and players will need to improve market share through brand visibility. Breweries will continue to leverage product innovation to remain competitive in the face of constrained pricing actions.

BULLS SAY

- Diversified product mix
- Efficient distribution network
- Customer loyalty and brand visibility
- Strong brand name
- Large market size

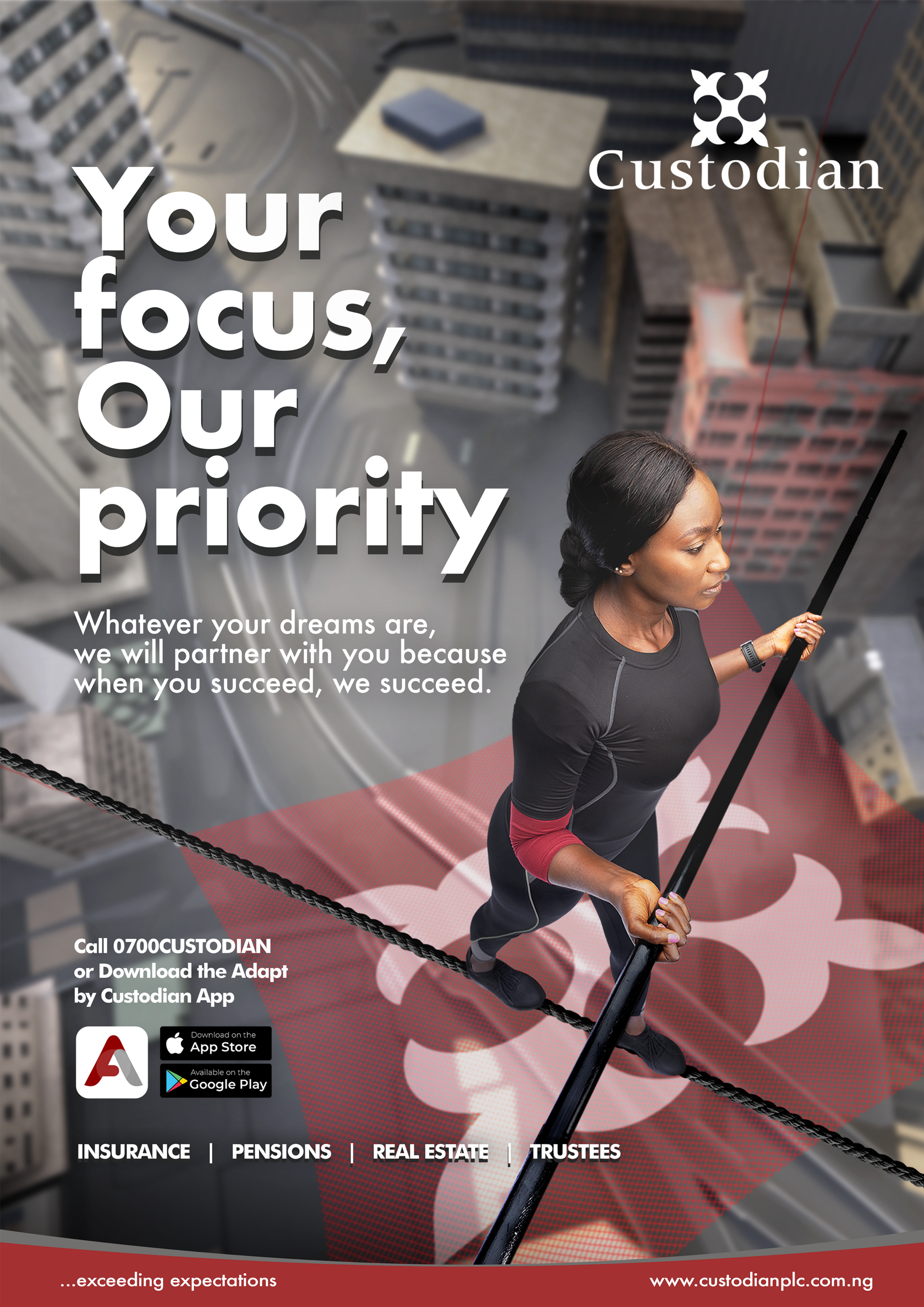
BEARS SAY

- Weak consumers' purchasing power
- Inconsistent policies
- Harsh operating environment
- Fx challenges
- High energy and input cost

OUTLOOK

Guinness Nigeria Plc has played a significant role in the Nigerian brewery industry, buoyed by investment in backward integration and a well-diversified brand portfolio. The company has continued to invest in strategies for manufacturing products that match consumers' expectations and has benefited from several government opportunities related to local content production and trade deals. This indicates that the company is well positioned to capitalize on a window of opportunities within the industry and is relatively immune from potential headwinds that could impair future business operations.

While major economic headwinds persist and weigh on profit margins through increased finance costs, Guinness Nigeria Plc faces the risk of currency devaluation due to its significant exposure to foreign debt as well as the risk of inflated interest expenses, particularly as interest rates have been rising. We expect a moderation in the company's capital structure in a bid to reduce exposure to debt and interest expense on intercompany loans. Notwithstanding, Guinness Nigeria's operations will continue to leverage its strong business model, brand recognition, and good product quality.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A PRiSM OUTLOOK - OCT'2023

Global

- The extension of oil output cuts by major producers Saudi Arabia and Russia is expected to keep global oil prices elevated above $90 per barrel. This will be supported by a post-pandemic rebound in economic activity - especially in China. The Energy Information Administration (EIA) forecasts tighter oil markets until year end with China's demand to grow by 2.2mbpd in 2023, reaching 101.8mbpd.

- The rise in oil prices will exert upward pressure on global energy costs, stoking inflationary pressures.

- While some central banks may pause their policy rate hikes, interest rates are expected to remain elevated, primarily due to the upside risks associated with inflation. Central banks in

Domestic

- Despite the rise in global oil prices, the country's sub-optimal oil production level (below OPEC quota of 1.74mbpd and 2023 budget benchmark of 1.68mbpd) is likely to weigh negatively on export earnings.

- This coupled with lower forex inflows will weigh on Nigeria's gross external reserves, which already plummeted by 2% in the last one month. The sustained depletion of the reserves will constrain the CBN's ability to intervene in the forex market. Consequently, the naira, presently at an all-time low N995/$, will likely experience further depreciation in the coming months, fueled by the surging demand for the dollar.

- However, higher oil prices could boost the FG's revenue in naira terms, further increasing FAAC allocations that climbed by 6.5% to N966.11bn in August.

- Moreso, Dangote refinery, which is set to begin in October, still imports oil as NNPCL $3bn crude-for-loan deal with AFREXIM puts pressure on local supply. Therefore, higher oil prices will exacerbate the naira woes and heighten the domestic price of PMS and other oil derivatives.

- The exchange rate pass-through effect to commodity prices will be more pronounced in September and October,despite the harvest season.

- The spiraling inflation, positive Q2'23 GDP growth and risks of capital flights will be major considerations at the monetary policy committee meeting (the first under the newly appointed CBN governor, Mr. Yemi Cardoso) set at a date yet to be announced. Against this backdrop, the committee will likely maintain a hawkish stance.