January 2023

Macroeconomic Review

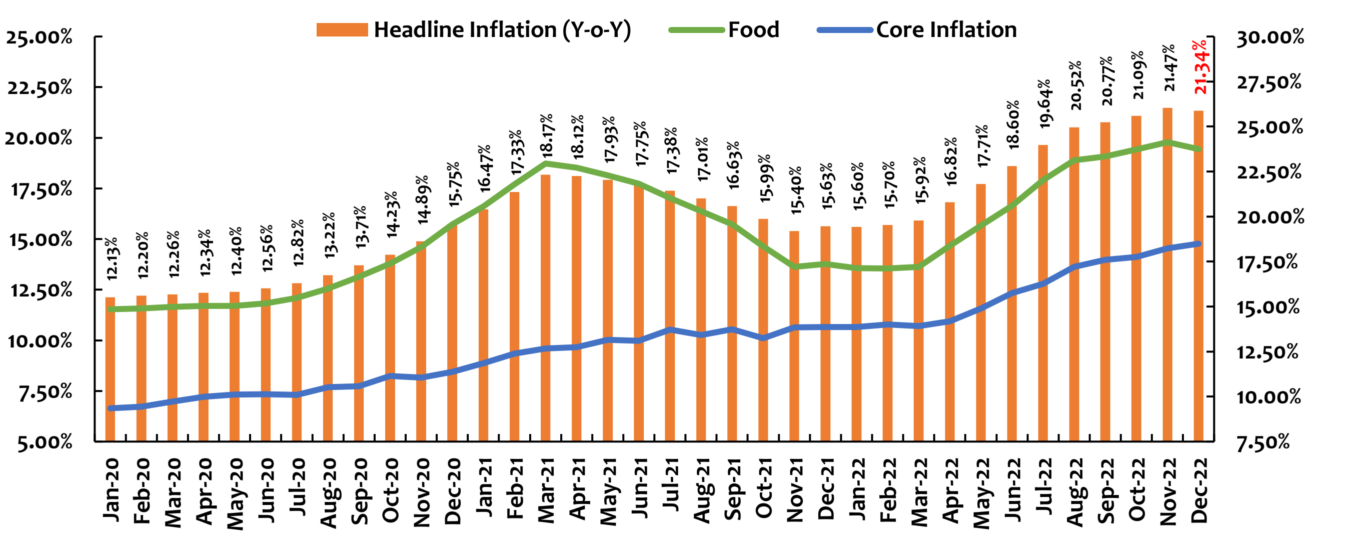
Nigeria's inflation - ***About time for "law of gravity"?***

After the sustained increase in Nigeria's inflation for the most part of 2022, Dec'2022 inflation turned out to be an outlier, as the National Bureau of Statistics reported a slight decline. According to the National Bureau of Statistics, Nigeria's headline inflation fell by some 0.13% to 21.34%, year-on-year, from the preceding month.

While a similar trend was observed in the food inflation, the core inflation witnessed an upward trajectory. To contextualize, the food inflation declined from 24.13% in November to 23.75%, year-on-year in December, while the core inflation exacerbated to 18.49% in December from 18.24% year-on-year in the preceding month.

Given that the prevailing factors contributing to Nigeria's inflation have not changed, we attribute the slight average decline in the headline inflation to a relatively low consumer spending during the festive period, as the soaring price of consumables influenced the usual high spending patterns of households.

Chart 1 – Headline Inflation, Food Inflation and Core Inflation



Source: NBS, AIICO Capital

Outlook:

As the high cost of energy persist, including the lingering fuel scarcity which has worsened inflationary pressures, we do not expect an improvement in the interim. To add, the currency depreciation and structural issues affecting the ease of supply-chain has not been adequately addressed. However, the naira swap, which has resulted to the CBN having a stronger control of currency circulation, could stabilize the inflationary pressures, and possibly moderate the pace of increase, but only to an extent, due to the dominating inflation drivers as sighted above.

<u>Nigeria's Monetary Policy Review</u> - ***MPC maintained a hawkish stance despite the drop in headline inflation.***

In Jan'2023, the Nigeria's Monetary Policy Committee had its first monetary policy meeting, where a hold stance or at best, a 50bps increase in benchmark interest was envisaged, given the fact that December's inflation slowed to 21.34% (13bps drop from Nov 2022 figure) and global central banks lowered the magnitude of rate hike in Dec 2022 (US Fed increased the benchmark interest rate by 50bps at its December meeting). However, the MPC instead increased the MPR by 100bps to 17.50%, citing the risk of sustained high headline inflation.

In addition, the committee expressed its satisfaction in the recent moderation in inflation and reiterated its strong intention to curb the soaring pace of inflation. Notably, all members of the monetary policy voted increase in the MPR, with 7 members for 100bps, 1 member for 150bps and 4 members for 50bps.

<u>Outlook:</u>

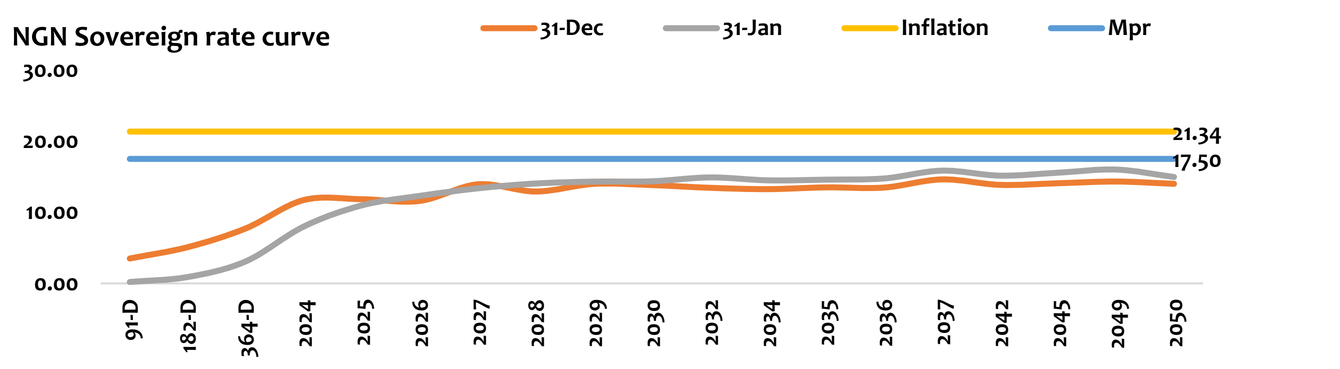
Going forward, the policy postures by the central bank further reveals a high possibility for an extended period of high interest rates or at least, another round of rate in the next meeting.

Fixed Income Market Review and Outlook

<u>Overview</u>

Divergent trends ensued in the local fixed income space, as buyside interest was seen across short-dated papers (treasury bills, OMO, CBN Special bills, Promissory notes, less than 3 years FGN bonds) mostly by banks and fund managers, while a mixed to bearish theme was witnessed in the FGN bonds market amid increased supply by the DMO. The Eurobond market also observed mixed sentiments but closed bearish amid dissatisfying reports by rating agencies, hawkish fed chatters and stronger than expected growth data, as it gives room for the US Fed to tighten further.

Chart 2 – Nigerian Sovereign Yield Curve



Source: CBN, FMDQ, AIICO Capital

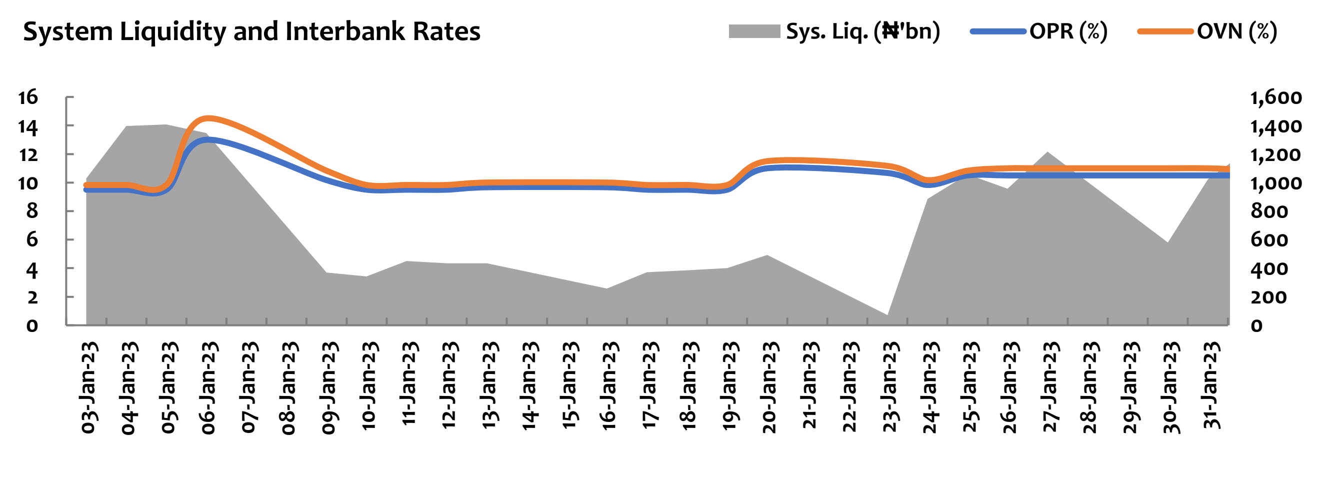
Money Market Review and Outlook – ***Buoyant system liquidity and lower interbank rates despite the increased MPR***

System liquidity remained elevated in the first month of 2023 due to significant inflows from bond coupons, FAAC credits, CBN Special bills and swap maturities. Although, the CBN conducted its discretionary mop-up exercises during the month using the CRR and Retail SMIS, system liquidity still averaged ₦709.62bn (vs ₦279.18bn in Dec 2022), and Overnight Policy Rate (OPR) and Overnight (ON) rates declined to 10.10% and 10.55% from 11.35% and 11.88% in Dec 2022.

During the month, the first monetary policy meeting was held, where the MPC increased the MPR by 100bps to 17.50%, a move that shocked a lot of market players. The CBN governor, Godwin Emefiele, reiterated at the meeting that the committee remained committed to tackling the soaring inflation and ensuring that the negative real return on investments is brought to near zero levels.

Money market activity post-MPC witnessed little impact from the rate hike, as interbank rates remained at its low levels amid ample system liquidity.

Chart 3 – System Liquidity and Interbank Rates



Source: CBN, FMDQ, AIICO Capital

Outlook: We expect the money market space to remain fairly liquid, though coupon inflows for Feb 2023 (₦77.5bn) is meagre compared to Jan 2023 (₦256bn). Expected maturities (OMO- c. ₦175bn; NTB - c. ₦480.57bn) and FAAC credits should also provide support to the liquidity status, thus, a slight increase in interbank rates is envisaged.

T-Bills Market Review and Outlook - ***Low rates across the curve amid elevated system liquidity and aggressive buying.***

The overall theme for the treasury bills market at the start of 2023 was bullish. Banks and fund managers scrambled to reinvest their idle cash in available short-dated instruments to avoid having their funds mopped up at 0% by the CBN and for statutory/regulatory reasons, respectively.

There was a significant decline in rates across the curves (NTB, OMO and CBN Special bills), as excess cash chased very few papers. At some point, investors switched to short-dated bonds (not more than 3 years) and promissory notes to get value, but offers were scanty. Though, rates improved occasionally after the usual CBN mop-up exercise, but it was always short lived as maturing investments (expected cash inflow) meant the week ahead was always bullish. It soon became a race of "how low can rates go", as banks and fund managers bought as low as 0.40% on the short end of the curve (2020 levels) and sub 2.0% on the long end.

For context, the NTB auctions (2) during month were bullish with heavy subscriptions recorded, and the DMO/CBN's allotment were not sufficient to cover the huge demand. The DMO took advantage of the "must-win" bids by the subscribers to borrow at the cheapest level possible. The total subscription for the month printed at c.₦1.43trn, while c.₦277bn was offered and same was allotted.

Overall, the average rate dropped by c.404bps M-o-M to close at 1.40%.

Table 1 – Nigerian Treasury Bills (NTB) Auction Result

JANUARY 2023 NTB AUCTION RESULT				
Tenor	**Dec'22 Close**	**Jan'23 Auc 1**	**Jan'23 Auc 2**	**Change M-o-M (bps)**
91	2.74%	2.00%	0.29%	(245.00)
182	7.15%	4.33%	1.80%	(535.00)
364	**8.49%**	**7.30%**	**4.78%**	(371.00)

Source: CBN, AIICO Capital

Outlook: Looking ahead to the expected supply in Feb 2023 (₦480.57bn), we expect rates to improve from Jan 2023 close. However, the body language of the CBN/DMO so far, suggests that they are more interested in skewing their borrowings this year to longer dated securities. As such, only the maturing size of investment (₦480.57bn) should be re-tapped by the DMO with no significant new borrowings. We also expect FAAC inflows to put pressure on rates, as well as the desperation of banks to reinvest the idle cash.

FGN Bonds Market Review and Outlook - ***Q1 2023 FGN bond issuance calendar set the pace for a mixed to bearish theme.***

The highlight of Jan 2023 FGN bonds activity was the release of Q1 2023 FGN bonds issuance calendar, where between ₦320bn and ₦400bn is expected to be borrowed from the domestic market across 4 bond maturities (2028s, 2032s, 2037s and 2049s) every month. It was no surprise however, as this aligns with market expectation, given the magnitude of the 2023 budget deficit.

Secondary market activity prior to the release of the calendar was mixed, with sideways interest recorded across the 2029, 2032, 2037, 2042 and 2049 maturities, though traded volumes were relatively meagre due to wide bid/ask spreads. Also, there were significant interest on 2024s and 2025s, given the significantly low rates in the treasury bills space.

The release of the calendar prompted c.70bps increase across the auctioned papers, as short-sellers took position ahead of the auction. There was a c.25% increase in repo contracts and costs touching nearly 6 kobo daily, as bets of a significant rise in marginal rates at the auction skyrocketed. However, some sort of moderation was seen across the curve as market players felt they had overdone the short openings. It was a mixed market thereafter, with large ticket players cherry-picking the attractive yields across the curve.

Building up to the auction, most players were skeptical about how the auction would playout, given that rates in the treasury space were at low levels and the system was awash with liquidity from FAAC and bond coupons. Thus, bids at the auction were submitted at "must win" levels especially by the Pension houses and Life insurance players. At the auction, the DMO utilized the opportunity of the heavy demand by mopping as much as possible, surpassing the expected ₦360bn, while managing their borrowing cost by maintaining the stop rate for the oversupplied 2037s at 15.80% and closing the 2049s 10bps higher.

Post auction market sessions were mixed to bearish due to the oversupply at the auction. Bids went off the roof but cooled off later as sellers were not willing to record losses on their auction winnings.

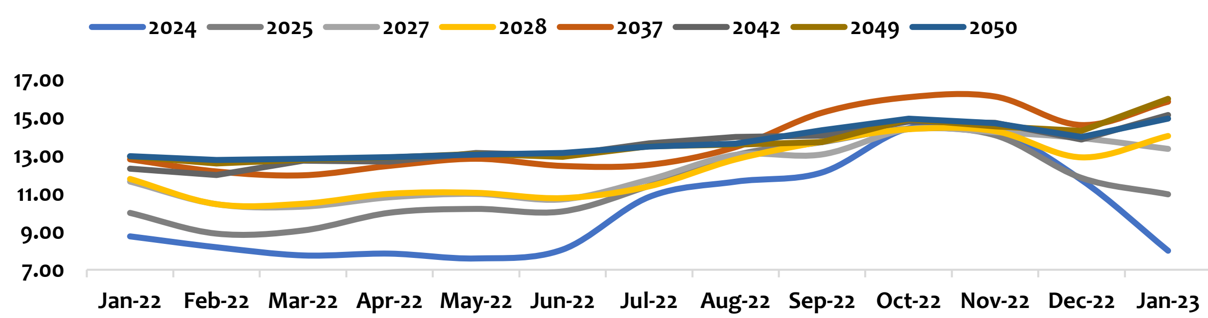
Overall, average mid-yield in the secondary market inched up by c.57bps M-o-M to close at 13.97%.

Table 2 – January 2023 FGN Bonds Auction Result

JANUARY 2023 BOND AUCTION RESULT						
Maturity	Offer (₦'bn)	Sub (₦'bn)	Allot (₦'bn)	Yield	Dec'22 Close	Change M-o-M (bps)
23-Feb-28	90.00	191.98	144.53	**14.00%**		0.00
27-Apr-32	90.00	91.14	65.04	**14.90%**	**14.75%**	15.00
18-Apr-37	90.00	260.47	232.47	**15.80%**	**15.80%**	0.00
26-Apr-49	90.00	261.57	220.57	**15.90%**		0.00
	360.00	**805.17**	**662.62**			

Source: DMO, AIICO Capital

Chart 4 – FGN Bond Yield Curve for Selected Maturities



Source: FMDQ, AIICO Capital

<u>Outlook:</u> With the next FGN bond auction 2 weeks away from the first (Feb 13), we anticipate another increase in marginal rates, albeit at a controlled level by the DMO. Secondary market should trade much higher amid low coupon inflows (c.₦77bn, could go higher depending on how much is supplied on 2028s at the auction).

<u>Eurobond Market</u> - ***Mixed to bearish theme amid lower sovereign ratings, hawkish US Feds, inflation and strong growth data.***

Positive equities opening ensured most of the notable Sub-Saharan African, Middle East and North African papers witnessed a bullish theme to start the year. It was basically one-way across Nigeria, Angola and Egypt; however Ghana witnessed a somewhat bearish affair amid the ongoing debt restructuring talks.

During the month, the Dec'22 Fed minutes were released, where no rate cut was anticipated this year, as the mandate to drive inflation to the desired level holds supreme. Thus, the Eurobond space witnessed a softer tone on the back of this, with selling interest observed across most African papers. Investors also kept a keen eye on the economic situation in Nigeria, after new data from the Debt Management Office showed that 80% of Nigeria’s Revenue Collection was consumed by debt payments in 2022.

Positive sentiments soon radiated the Eurobond space, as greens were recorded across the African papers (Sovereigns and corporates), driven by China’s reopening of trade and expectations of slower rate hikes. The dollar weakened, stocks extended global gains in risk assets and oil rallied. The bullish momentum was intensified by the expected decline in US inflation, as it slowed to 6.50% (prev. 7.10%) with Core inflation printing at 5.70% (prev. 6.00%).

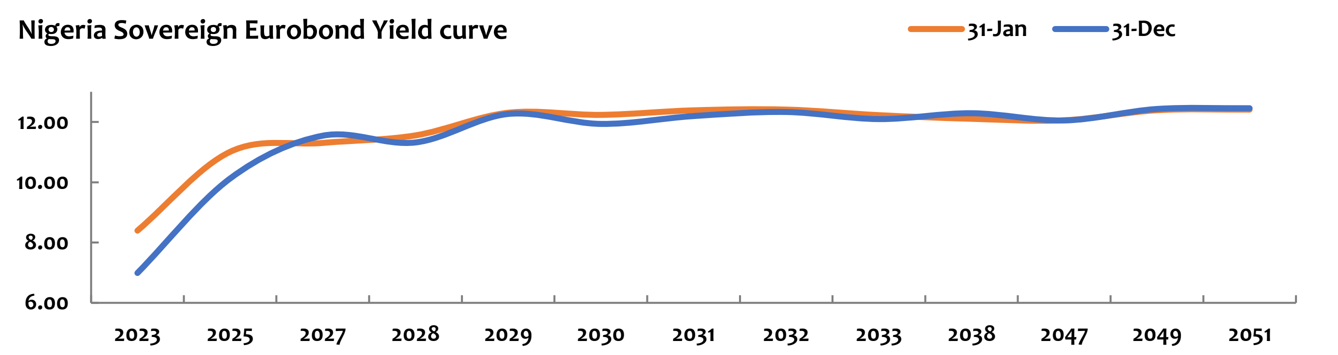
The month closed on a mixed to bearish note amid poor growth data from China, valid concerns on economic outlook as highlighted in U.S’ data, hawkish US Fed chatters, declaration of Ghana 2026s bond as default by S&P Global Ratings, stronger than expected Q4'2022 GDP (2.90% vs Est. 2.60%) and Moody's latest downgrade of Nigeria's long term foreign debt rating to Caa1 from B3 (stable outlook).

Overall, the average mid-yield across Nigeria’s Eurobond curve increased by c.21bps M-o-M to close at 11.75%.

Other notable information:

- *Angola central bank cut its benchmark interest rate to 18% from 19.5%.*
- *US Non-farm payrolls printed higher than expected (223k vs Est. 203k), while the Unemployment rate closed at 3.50%.*
- *Ghana extended its local debt exchange for the 4th time to Feb 7, 2023.*
- *Ghana’s Dec’22 inflation rose to 54.10% (Est. 51.80%).*
- *Ghana banks agree to a proposed 5% coupon payment in domestic debt swap program, and 9% coupon on 12 new issues.*
- *Ghana raised its benchmark interest rate to 28.00% (Est. 29.00%) , while Kenya maintained its benchmark rate at 8.75% (Est. 9.00%).*

Chart 5 – Sovereign Eurobond Yield Curve



Outlook: At the latest FOMC meeting, where an expected 25bps hike happened and the tone of Fed Chair Powell indicated that the pace of rate hikes might be slowing in the coming months, we expect renewed buyside interest across the African papers, especially Angola, Egypt and Nigeria while investors continue to monitor the developments regarding Ghana's debt restructuring talks. However, the recent stronger than anticipated US Non-Farm Payrolls (571,000 vs. Est. 188,000) and Unemployment rate (3.40%) might tilt the market to a bearish thme, as it suggests that there is no recession risk on sight and the Fed can still tighten further.

Foreign Exchange Market Review and Outlook - ***FX reserves decline further; Naira held steady against the dollar at the I&E window.***

Activity in the FX market was quite slow to start the year with minimal volatility observed at both the official and unofficial markets, amid trifling intervention by the CBN through the bi-weekly Retail SMIS amongst others. The exchange rate closed the month at an official rate of ₦461.5/$1 (same as Dec 2022 close) at the Investor and Exporter (I&E) window with NAFEX closing at ₦461.3/$1. However, at the unofficial market, the exchange rate closed between ₦740/$1 - ₦745/$1 on cash trades, while Inflows closed at ₦753/$1. The Gross external reserves closed at $37.02bn compared with $37.08bn as at close of 2022.

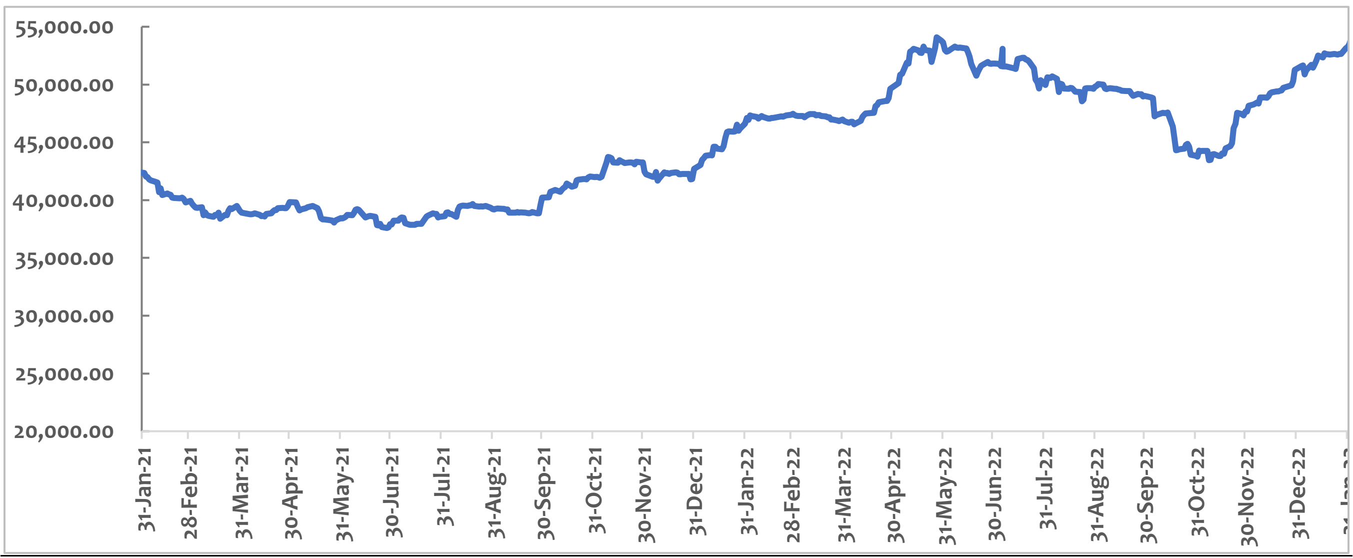
Outlook: The election in Feb 2023 may see a heightened demand for FX by political personnel, further weakening the Naira. Also, If the result of the election sways in favour of the ruling party, there is a likelihood of another round of mass exodus of Nigerian youths to foreign countries in pursuit of greener pastures, putting a strain on Naira's recovery.

Equities Market Review and Outlook

Equities Market Performance in January – ***Capital Gains for Nigerian stocks despite election concerns***

The Nigerian stock market closed the first month of the year on a bullish note, as the All-share Index (ASI) advanced by 3.88% (c. 1,987.61bps) since the start of the year to 53,238.67 points. In the same vein, Market Capitalization which opened the trading year at N27.92 trillion, appreciated by N 1.08 trillion to close the month at N28.99 trillion.

Chart 6 – NGX ASI YTD Performance



Source: NSE, AIICO Capital

Positive performance Across Sectors

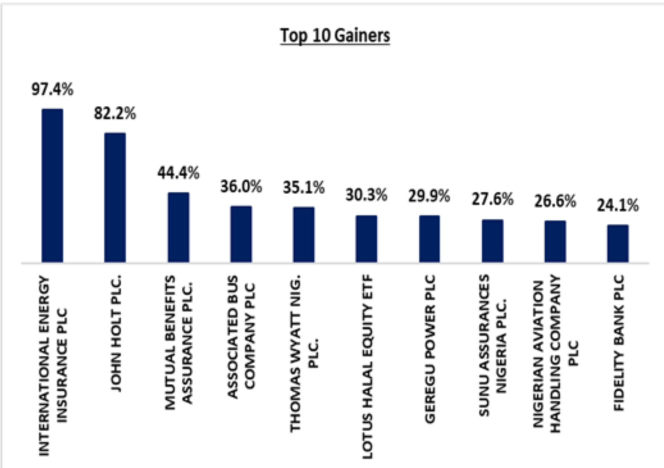
Performance across all sectors were positive at the end of the month, as the NGX Banking index recorded the highest rise during the month with a gain of 7.51%, the NGX Consumer Goods index followed with a monthly gain of 5.64%. The NGX Oil &Gas and NGX Industrial Goods indices also recorded monthly gains of 5.41% and 2.14% respectively.

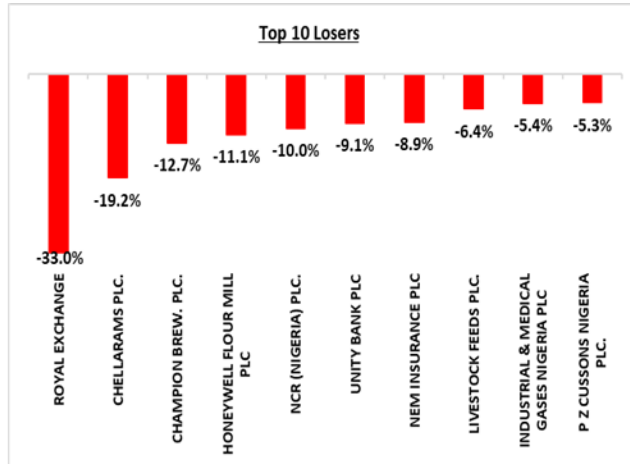
Table 3 – Sector Performance

	MTD	YTD
NGX ASI	↑3.88%	↑3.88%
NSE Banking Index	↑7.51%	↑7.51%
NSE Insurance Index	↑5.36%	↑5.36%
NSE Industrial Goods Index	↑2.14%	↑2.14%
NSE Consumer Goods Index	↑5.64%	↑5.64%
NSE Oil & Gas Index	↑5.41%	↑5.41%

Source: NSE, AIICO Capital

Chart 7 – Top 10 Gainers and Top 10 Losers in September





Source: NSE, AIICO Capital

Outlook

Sentiment has remained positive despite Moody's downgrade of Nigeria, due to worries about the impending general elections, particularly considering the recent surge of violence around the country, as well as rising governmental indebtedness, among other issues. Although caution is necessary considering the upcoming elections, we predict that positive attitude will endure.