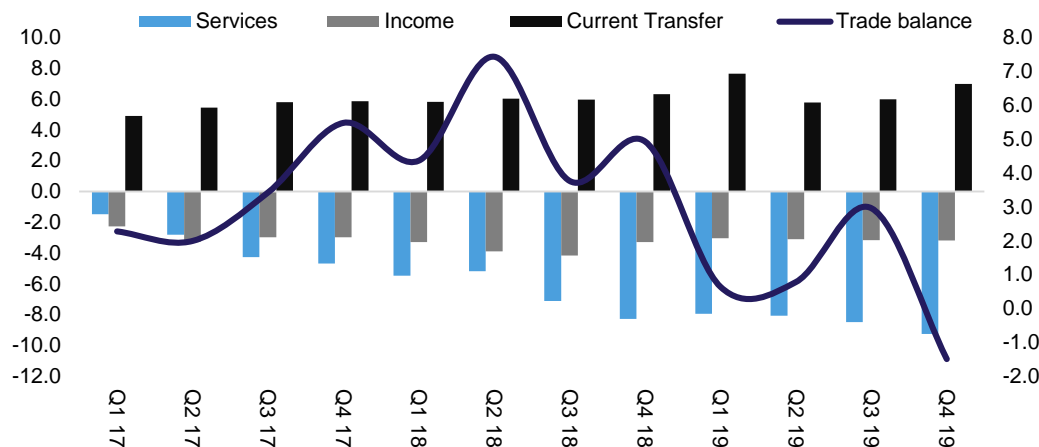


Monthly Economic Insights

Current Account: Deficit on the Run as Pressure Mounts

The current account balance recorded a combined deficit of \$17 billion in 2019 compared with \$3.9 billion surplus in 2018. Specifically, the deficit of \$7.0 billion in Q4 19 more than exceeded our estimate of \$2.7 billion following the appearance of the first trade deficit in thirteen quarters of \$1.5 billion (estimate of \$861 million surplus) and a wider than expected services deficit of \$9.26 billion (estimate of \$6.53 billion). On the balance of trade, Q4 19 witnessed a surge in non-oil import, even as oil imports slowed. Compared to average non-oil import of \$12 billion over Q1 to Q3 19, Q4 standalone was \$15 billion to push overall import to \$17.2 billion (+17% QoQ and +75% YoY). Interestingly, the cumulative non-oil imports of \$51 billion over 2019 (oil import of \$11 billion) far exceeded \$29 billion in 2018 (oil import: \$11.6 billion). While we reckon that ongoing capacity expansion in oil refinery and railway construction magnified the numbers over 2019, we are also surprised about the scale of growth in manufactured goods import by 60% YoY. On the other hand, export over Q4 fell by \$1.4 billion to \$14.79 billion following decline in oil export by \$1.5 billion. With cumulative 2019 export of \$64.98 billion (+6.14% YoY) compared to total import of \$62.11 billion (+52.4% YoY), the trade surplus moderated to \$2.87 billion compared to \$20.47 billion in 2018.

Figure 1: Historical Current Account Components (\$'billion)



Source: CBN, NOVA Research

As mentioned above, the services deficit deepened over Q4, with cumulative 2019 deficit of \$33.8 billion (2018: \$26 billion). Personal travel and professional & business services accounted for bulk of the increase in services deficit over 2019. On the positive, while income deficit narrowed to \$12.5 billion (Q4 19: \$3.2 billion), current transfer surplus leapfrogged to \$26.4 billion (Q4 19: \$7 billion), even as workers' remittances declined marginally to \$23.5 billion.

The Month's Key Points

- [Current Account: Deficit on the Run as Pressure Mounts](#)
- [FPI Outflows Escalate](#)
- [Breakup in Supply Chain Marches Inflation Upwards](#)

Other Readings

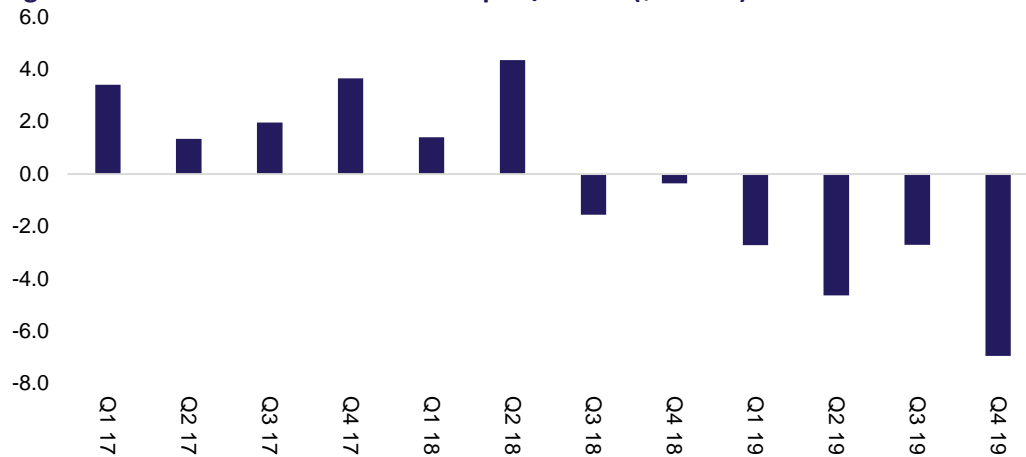
- [Fiscal Position Getting Critical](#), 27 March
- [MPC Preview: Tough Times... Limited Options](#), 24 March
- [Breakup In Supply Chain Portends Major Risk For Price Stability](#), 17 March
- [Global Shocks Alters Nigeria's Short Term Outlook](#), 16 March
- [Monthly Oil Market Update](#), 12 March
- [Q4 19 GDP – Positive Surprise, But Sustainable?](#), 24 February

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Figure 2: Historical Current Account Surplus/Deficit (\$'billion)



Source: CBN, NOVA Research

Over 2020, the depressed global crude oil prices amidst pressured demand pose major risks for the export and the trade balance. Intuitively, we reckon that sustained pressure on oil revenue will result in CBN implementing some administrative measures to limit the scale of imports (especially, non-oil import) and even services demand as witnessed in 2016 prior to the introduction of personal travel and business travel allowances. Beyond CBN actions, the spread of Covid-19 across major economies – even as we expect a successful containment without major escalation beyond Q2 – will have a major impact on travel and related services for the rest of the year. Also, given the expected lower return on investment and feedthrough of the global shock on individual income, we model lower income deficit and workers' remittances respectively. As in the table below, our base case models a trade deficit of \$9.1 billion (compared to 2019 surplus of \$2.9 billion), services deficit of \$20.1 billion (compared to 2019 deficit of \$33.8 billion), income deficit of \$10 billion (compared to 2019 deficit of \$12.5 billion) and current transfer surplus of \$19.6 billion (compared to 2019 surplus of \$26.4 billion). All told, we expect current account deficit of \$19.6 billion in 2020, exceeding 2019 level of \$17.0 billion.

Figure 3: Historical and Forecast Current Account Components

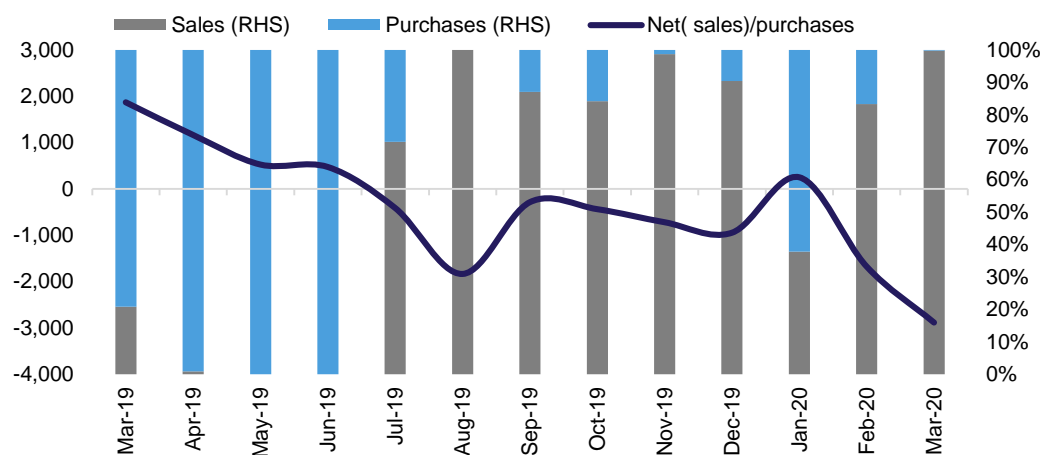
(\$' Million)	2017	2018	2019	2020 Estimates		
				Bear	Base	Bull
<i>Oil production (mbpd)</i>	1.90	1.92	2.02	1.94	2.05	2.10
<i>Oil price (\$/bbl)</i>	54.09	74.69	65.81	31.42	38.53	45.64
<i>Crude Oil Export</i>	42,297	56,555	54,511	25,314	32,803	39,804
<i>Non-Oil Export</i>	3,521	4,666	10,466	4,866	6,306	7,651
Total exports	45,817	61,221	64,978	30,180	39,108	47,455
<i>Non-Oil Import</i>	24,514	29,187	51,085	39,650	38,759	36,045
<i>Oil Import</i>	8,155	11,566	11,025	9,642	9,425	8,766
Total Imports	32,669	40,754	62,110	49,292	48,184	44,811
Balance of Trade	13,148	20,467	2,868	-19,112	-9,076	2,644
Services Deficit/Surplus	-13,234	-26,066	-33,761	-22,075	-20,068	-18,664
Income Deficit/Surplus	-11,510	-14,658	-12,492	-10,950	-9,986	-9,275
Current Transfer Deficit/Surplus	21,996	24,134	26,369	18,194	19,564	21,520
Current Account Deficit/Surplus	10,399	3,878	(17,016)	(33,943)	(19,566)	(3,775)
CA % of Nominal GDP	2.32%	0.93%	3.61%	8.81%	5.05%	0.98%

Source: CBN, NOVA Research Estimates

FPI Outflows Escalate

The apex bank recorded its highest monthly intervention sales at the IEW in March, with the gross external reserve depleting by \$1.0 billion to adjusted level of \$34.0 billion. The apex bank net FX sales totaled \$2.9 billion, compared to net sale of \$1.7 billion in February. Notably, outflows during the month amounted to \$3.5 billion (-3% MoM), foreign inflows was a meagre \$335 million, while local supplies (ex-CBN) was only \$819 million with the market recording a deficit of \$2.7 billion. Over Q1 2019, foreign inflows summed to \$3.8 billion, outflows of \$9.2 billion with the apex bank net sales of \$4.3 billion (net purchase of \$4.3 billion in Q1 19). The lower foreign inflows amidst sizeable selloffs largely reflect the impact of the global risk-off sentiment and the dwindling reserves, both of which have limited the rate of portfolio inflows, even as more funds exit the economy.

Figure 4: CBN activity at the IEW

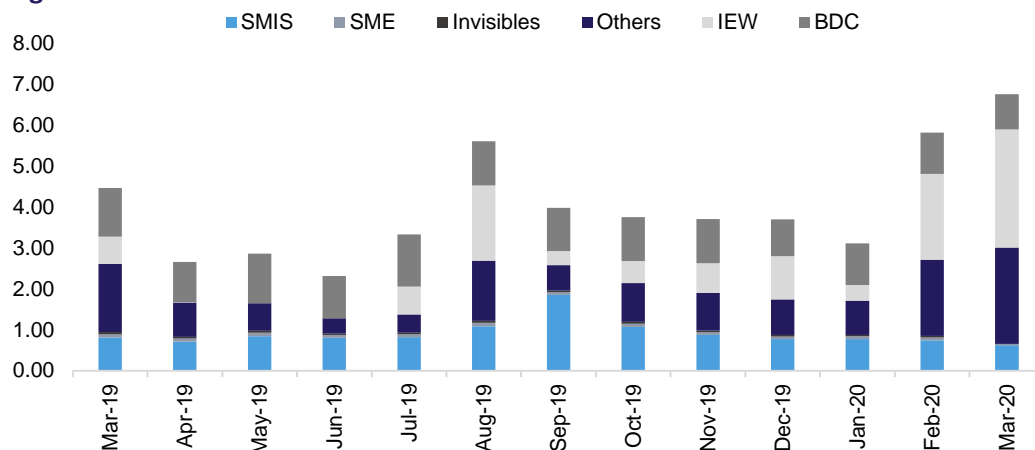


Source: FMDQ, NOVA Research

Notably, activities at OMO auctions in March depicted limited foreign portfolio participation. While the apex bank offered a total of N250 billion in response to maturing instruments of N671 billion (with foreign holdings of 50%), subscription came in at just N120 billion which largely suggest low FPI participation. Reflecting the mounting pressure on the exchange rate and gross reserve, the CBN initiated adjustments to the NAFEX and BDC rates to synchronized level of N380/\$, and upward revision of the official rate to N359.5/\$ (from N307/\$) to support higher oil revenue in Naira terms. Post the adjustment, the NAFEX rate has further depreciated, closing the month at N384.45/\$.

At other segments, the CBN sales increased by 8% MoM to \$4.0 billion in March. Sales to the SMEs, Invisibles and SMIS (retail and wholesale) windows declined 23% MoM to \$659 million due to the CBN's rationing of dollars and DMBs lowering bids to avoid unusual debits by CBN for bidding excessively at SMIS auctions. Elsewhere, non-auction and BDC sales increased by 12% MoM to \$3.4 billion. Overall, CBN intervention sales across windows increased by 19% MoM to \$6.9 billion. Even with the dollar rationing at the interbank and SMIS, it is our understanding that the apex bank is yet to deliver on most sales in the month of March, which is why we refrain to interpret these sales as actual cash transactions. save for the IEW and BDC sales.

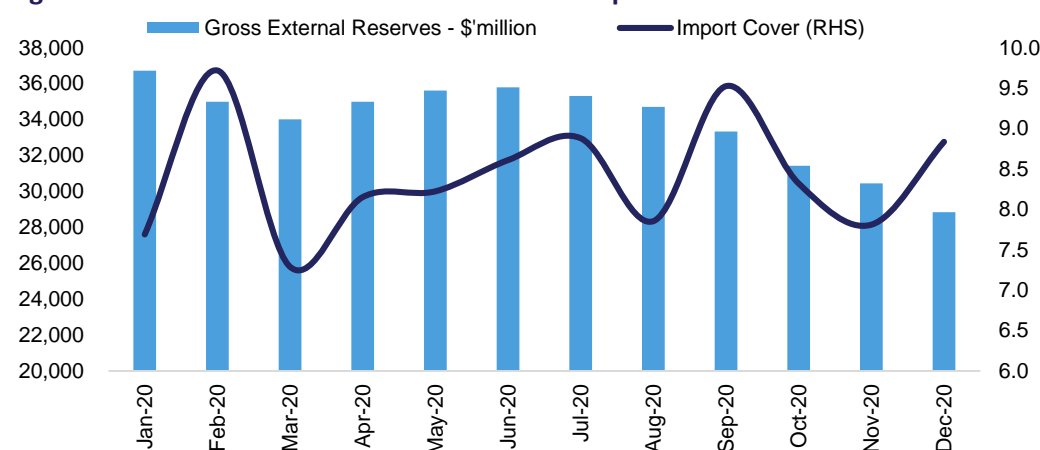
Figure 5: CBN intervention sales across markets



Source: CBN, FMDQ, NOVA Research

As mentioned above, the apex bank initiated upward adjustments to both the NAFEX and official rates to limit pressure on the reserves in March. With limited inflows in sight and reduced avenues to control outflows, we do not see the adjustments having any material impact on the reserves (See report: [Recent Price Adjustment Will Have Limited Impact](#)). As such, we believe the only option that will have any meaningful impact on the reserve is an outright floating of the exchange rate with intermittent intervention to avoid unnecessary speculative attacks. That said, we believe current breakup in supply chains and the effect of the ongoing COVID-19 pandemic across countries would have resulted in a sharp decline in import demands and even services.

Figure 6: Forecast Gross External Reserves and Import Cover



Source: CBN, NOVA Research Estimates

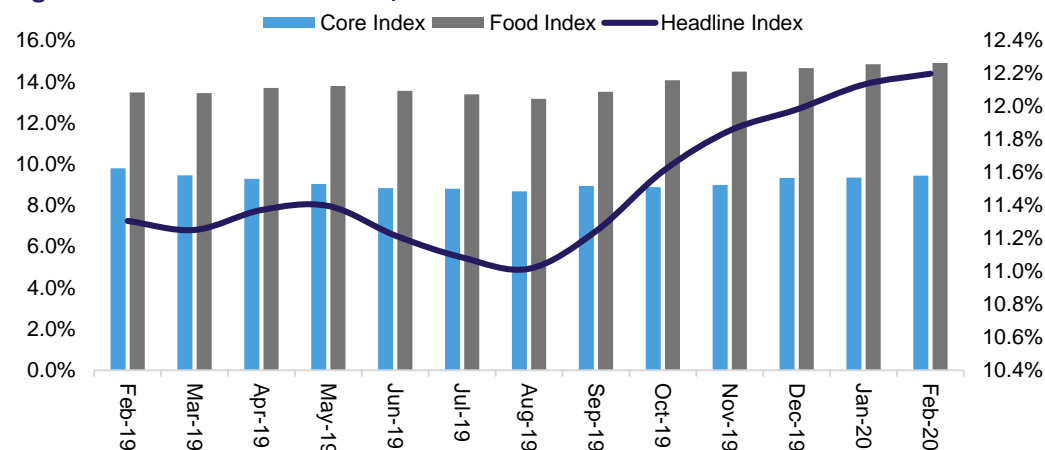
In modelling the reserve position over the rest of the year, while we have adjusted expected oil inflows to reflect the depressed oil price and the absence FPI inflows, we also note the impact the suspension of sales to BDCs will have on CBN FX sales. For every month the apex bank defers sales to BDCs, about \$1.1 billion is saved. Also, the minimal demand for services (especially business and personal travel allowances) and imports could also halve related FX demands. As such, the major pressure for the reserves are offshore holdings of maturing fixed income instruments, which is estimated at \$10.6 billion between April and December.

Assuming 100% of the offshore holdings are repatriated (which is a worst case scenario), and absence of BDC sales in April and May with a resumption of sales in June (amidst limited import and services demand), the gross external reserves could end the year at \$28.8 billion. However, given the scale of fixed income sales by offshore investors prior to maturity, the timing of the repatriation might defer from our monthly expectations based on the maturity profile. While the partial price adjustment and subsequent depreciation suggests a year to date weakening of the NAFEX rate by 5.5%, it is still below our fundamental based purchasing power parity rate of N405/\$.

Breakup in Supply Chain Marches Inflation Upwards

Month-on-month inflation expanded at a slower pace in February by 0.79%, coming below 0.82% MoM in January and our forecast of 0.85% MoM change. The slower expansion compared to the prior month was largely mirrored in both the food and the core index. The food index declined 12bps MoM to 0.87% (to mark the slowest MoM change in more than twelve months) following a sharp decline in processed food by 60bps to 0.99% which was further supported by 7bps softness in farm produce to 0.86% (a fallout of buoyant market supplies of tubers, millet, rice, and maize remain despite the conclusion of the main harvest season). For the Core index (-9bps MoM to 0.73%), the decline stemmed from most constituents, including Clothing & Footwear (-12bps to 0.76% MoM), Health (+19bps to 0.80% MoM), Transport (-5bps to 0.75% MoM) and HWEGF (-3bps to 0.54% MoM).

Figure 7: YoY Trend in Headline, Core and Food Inflation Trend

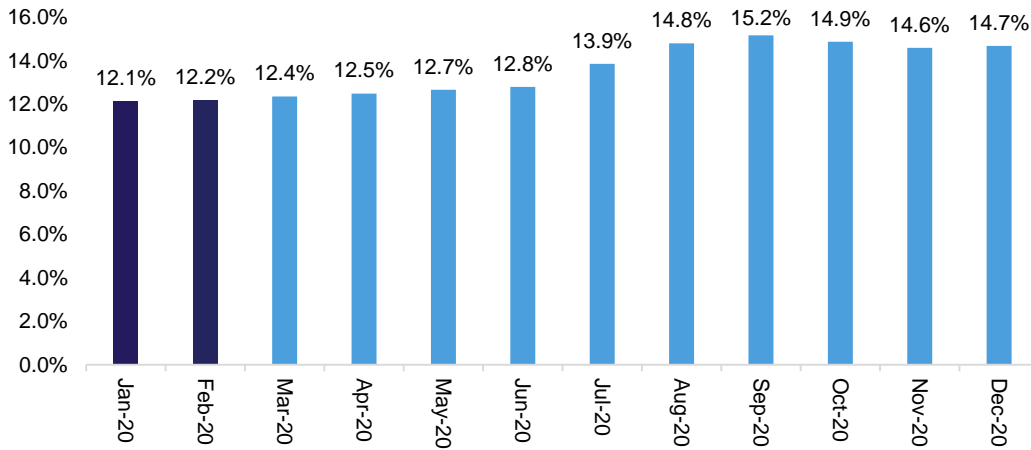


Source: NBS, NOVA Research

Coming below our estimate, inflation rate expanded by 12.20% (coming ahead of January level of 12.13%) to beat our estimate by 7bps. The expansion emanated from increases in both the core and food index. Surprisingly, while the core index (9bps to 9.43% YoY) had been muted in the prior month, it increased at a much faster pace compared to the food index in the month of February, following increases in HWEGF (+21bps to 7.81%), Transport (+12bps to 9.43% YoY), Health (+8bps to 9.94% YoY) amongst others. The food index (+6bps to 14.90% YoY) continues to reflect the low base of the prior year, which is further espoused by the feedthrough of the land border closure on food prices (with a gradually fading impact as seen in the MoM movement).

Events over the last two weeks in March to a large extent changed our view of price movement over the rest of the year. While we had stated that the disruptive impact of a breakup in the supply chain would transmit to temporary higher prices (due to feedthrough from scarce imported commodities and higher demand for local substitutes), the abrupt adjustment to the exchange rate and jump in prices of essential items (due to the lockdown) will further magnify the upside in prices. However, we note the downward adjustment to PMS prices, but we believe the impact will be muted since it was not immediately effected across most states and yet to reflect in downward adjustment to transportation expense. All told, we expect the consumer price index to expand by 0.93% MoM, with headline YoY expanding to 12.36% YoY in March. Beyond March, the delay in the effective date for the increase in electricity tariff to July still played well with our earlier model. But we expect the impact of the exchange rate depreciation, higher transportation cost of essential items due to lockdown and expected fluctuation in PMS prices due to monthly price modulation (as crude oil prices trend higher) to have a combined effect on inflation for the rest of the year. All told, we revised average inflation rate for 2020 to settle at 13.55% on our base case.

Figure 8: Forecast 2020 inflation trend



Source: NBS, NOVA Research Estimates