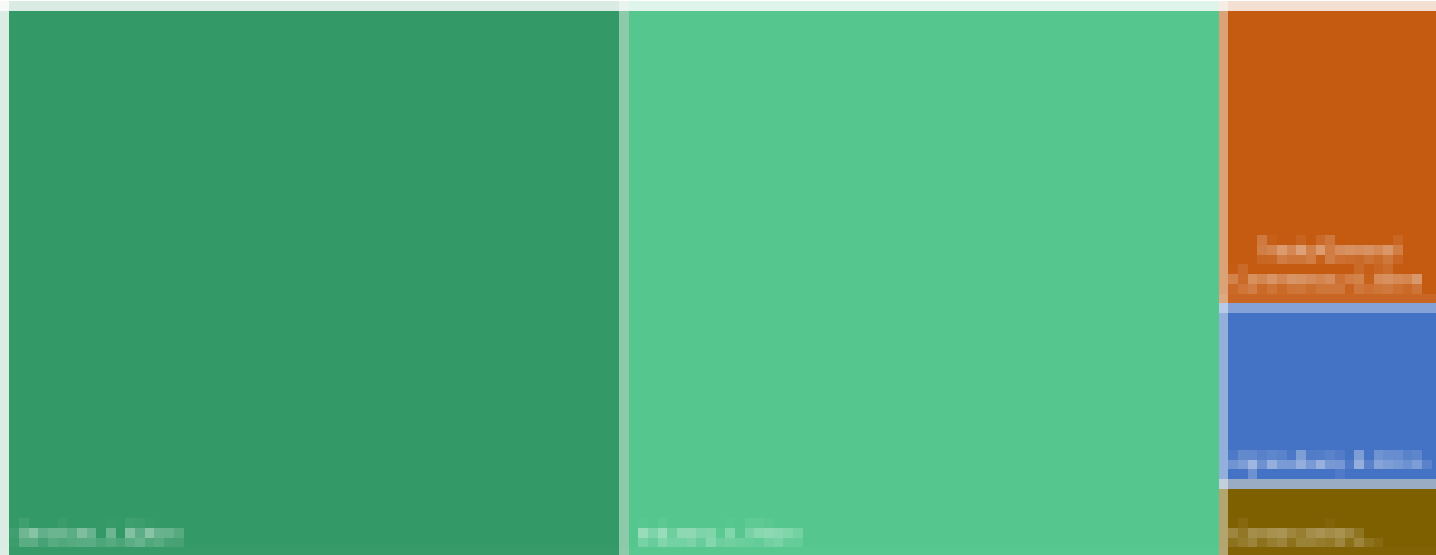


**Chart 29: Sectoral Representation of Credit to the Private Sector in 2022**



Source: CBN, Meristem Research.

*In 2023, we expect a modest growth in money supply. This is hinged on the contractionary monetary stance and the recent currency management policies such as the redesigning of the naira notes and the limit on cash withdrawal.*

*The increase in the cash reserve ratio to 32.50% is expected to limit the extent of credit that can be advanced by the deposit money banks in 2023. Furthermore, the expectation of a slowed growth might inform a cautionary approach to lending to the private sector in order to prevent a spike in the Non-Performing Loan ratio, which was at 4.80% as of September 2022. Thus, we expect a moderate growth in credit to the private sector in 2023.*

*On the other hand, credit to the government is likely to increase significantly. This view is premised on the huge deficit in the 2023 budget, the perceived credit worthiness of the government, and the limited financing window from the international capital market.*

# Inflation

## Lingering Challenges Steer Inflation Northward

Like most SSA countries, the inflationary pressures witnessed in the global economy trickled down to the inflationary environment in Nigeria. These coupled with domestic challenges propelled headline inflation northward, settling at 21.47% YoY in November 2022 (vs. 15.60% in January). We also note that imported inflation averaged 17.80% as of November 2022 (vs 17.04% in 2021). We expect the headline Inflation rate to average 18.78% by December 2022 driven by the increase in both the food and core index.

The food index grew by 21.46% YtD (November 2022), steered by the rise in food items such as bread, cereals, tubers, and oil. Food inflation maintained an upward trend despite moderation in global food prices since March 2022 and post-harvest supplies during the year. In our view the structural challenges (*poor infrastructure and storage facilities, incidences of flooding and insecurity*) which deterred agricultural activities and the aforementioned increase in imported inflation led to the uptrend in prices of food items.

Similarly, the core index expanded by 16.93% YtD (November 2022), piloted by the increment in gas, liquid & solid fuels prices and transportation costs (road and air). According to the National Bureau of Statistics (NBS), the average prices of Premium Motor Spirit (PMS), diesel, and kerosene increased by 20.81% YoY, 191.94% YoY, and 145.68 % YoY to NGN202.48, NGN808.87, and NGN1,083.87 respectively as of November 2022. This mirrors the jump in crude oil prices, as it averaged USD100.61/bbl as of November 2022 (vs USD70.95/bbl in 2021) translating to the increased cost of petroleum by-products. FX illiquidity and Naira depreciation also exerted pressure on the cost of energy and other imported items.

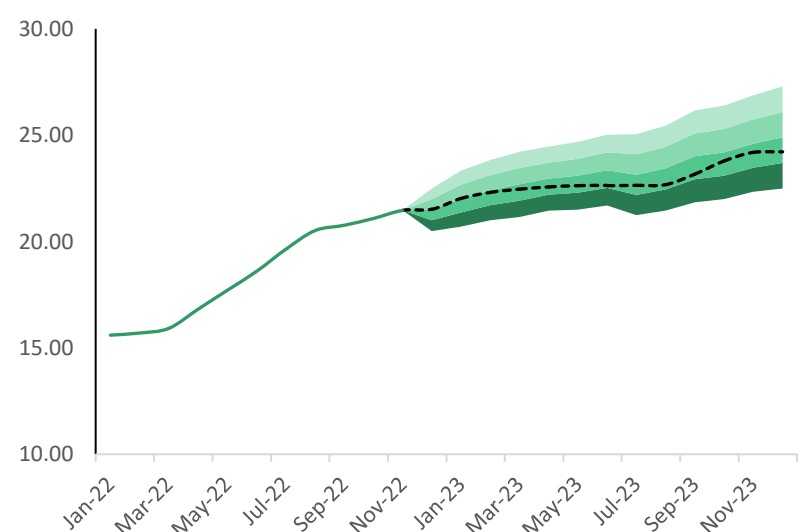
Given the positive correlation between money supply and inflation, it is important to highlight that the increase in the money supply in 2022 also influenced the persistent rise in the headline inflation rate.

## No Moderation in Sight

*We expect inflation to remain elevated for the most part of 2023. This is hinged on a number of factors: the lack of a clear path to end the lingering fuel scarcity; the possible removal of fuel subsidies in the second half of the year; the persistent FX illiquidity issue; and high spending ahead of the general elections. However, we do not expect a significant jump in the inflation rate due to the high base effect from 2022.*

**We forecast an average inflation rate of 22.95% in 2023 in our base case scenario (with a forecast band of 21.58% - 26.15%), compared to an estimated average of 18.78% in 2022.**

**Chart 30: Trend in Inflation % (Historical and Forecast)**



Source: NBS, Meristem Research.

# Monetary Policy

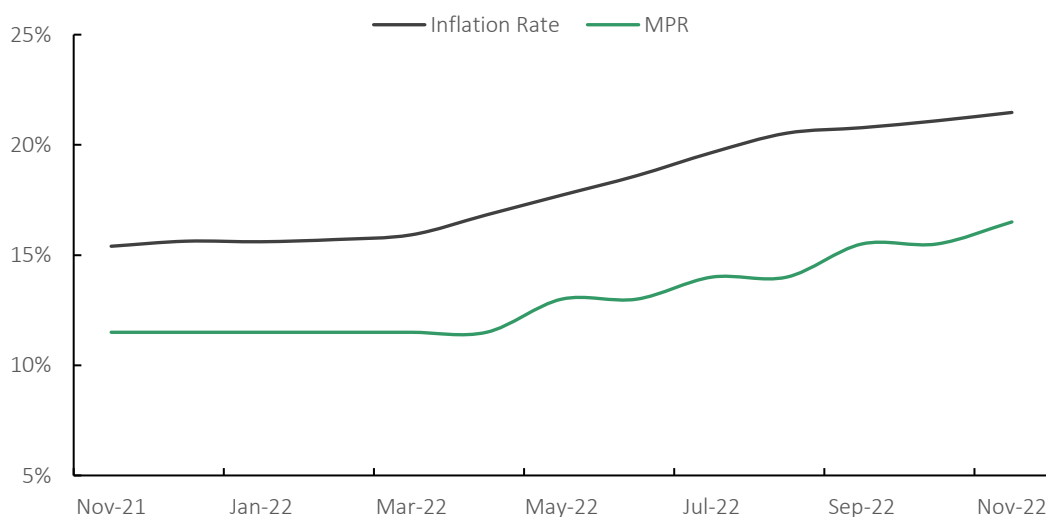
## Further Tightening In Sight

In a dramatic shift in policy stance, the heightened inflationary environment led the Monetary Policy Committee (MPC) to hike the Monetary Policy Rate by 500bps cumulatively to 16.50%. In addition, the MPC raised the Cash Reserve Ratio (CRR) by 500bps to 32.50% at its September meeting with the motive of reducing the money supply.

A major hindrance to the effectiveness of monetary policy in Nigeria however has been the volume of money outside the banking system. The need to reduce the demand-pull inflation fuelled by this informed the CBN’s redesigning of the NGN200, NGN500, and NGN1,000 notes. Furthermore, to achieve the stated objective, the Apex bank instituted a new weekly cash withdrawal limit : NGN500,000 for individuals and NGN5.00mn for corporates across all channels.

*Over the course of the previous meetings, the posture of the MPC is to keep the rate cycle going until at least some moderation to inflation is observed. Given our outlook for inflation to remain high, we see the possibility of further MPR hike by another 200bps in 2023. For the currency redesigning, we do not think this would help much in bringing inflation under check in the near term. However, we think it is a positive in driving the CBN’s cashless policy.*

**Chart 31: Movement of Inflation and Monetary Policy Rate (%)**



Source: NBS, CBN, Meristem Research.

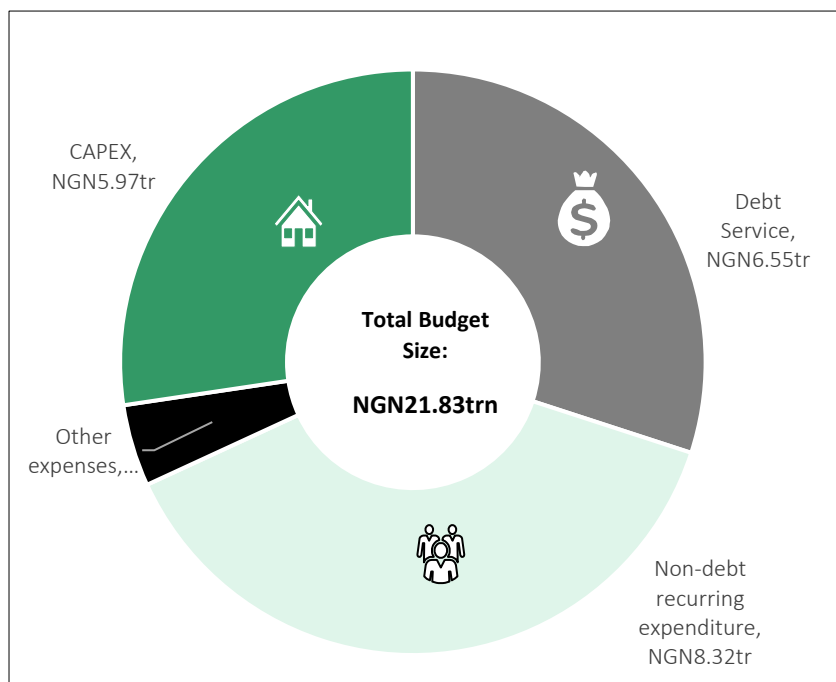
# Fiscal Policy

## The 2023 Budget: "Budget of Fiscal Sustainability and Transition"

The Federal Government of Nigeria (FGN) budget for 2023, which also happens to be the last budget of the present administration was recently approved by the National Assembly. Dubbed the "Budget of Fiscal Sustainability and Transition", the total budgeted expenditure is NGN21.83trn which is 22.50% higher than the 2022 budget (NGN17.82trn). The projected revenue is NGN10.50trn, translating to a budget deficit of NGN11.33trn (or 51.90% of the total budget).

According to the approved budget, capital expenditure (NGN5.97tr) represents c. 27% of the total budget size while non-debt recurrent expenditure and debt service are expected to take c. 38% and c. 30% respectively. In our recent macroeconomic [note](#) we evaluated the assumptions of the budget. We also discussed the performance of the last five FGN budgets including that of 2022 up till August. In our opinion, the assumptions underlying the 2023 budget have already set it on the path of not being achievable.

**Chart 32: Breakdown of the 2023 FGN Proposed Budget**



Source: Budget Office, Meristem Research.

**Table 5: Assumptions Underlying the Approved 2023 Budget**

Parameters	Value
Oil Price	USD75pb
Oil Production	1.69mbpd
Inflation Rate	17.16%
GDP Growth Rate	3.75%
Exchange Rate	NGN435.57/USD

# Debt Profile

## Mounting Debt Triggers Rating Downgrade to Near-Junk

In 2022, one of the major issues of concern was the precarious state of Nigeria's public finance. As debt was mounting, so was debt servicing while government revenue, (especially from oil which historically makes up over half of FGN revenue) was dwindling. This has raised concern about the fiscal strength of Nigeria being under duress. Official data from the Debt Management Office (DMO) shows that the FGN total domestic debt stock was NGN21.55trn as of September 2022, representing a net increase of NGN2.31trn in 2022 standalone (or 12.00% higher than December 2021 level). Adding the external obligations of NGN17.15trn (or USD39.66bn) brings the FGN's total debt stock to NGN38.70trn. Currently, FGN debt (which makes up over 85% of total public debt in Nigeria) is c. 21% of GDP (lower than the self-imposed limit of 40%), however, the rising debt level could push this significantly up in the near term. Moreover, adding the Ways and Means balance of c. NGN24trn immediately raises the debt-to-GDP ratio higher to c.35%.

### The Rising Concern on Debt Burden

With the mounting debt balance comes higher debt servicing need which has been a major pain point for Nigeria. Our analysis of data from the FGN puts average interest rate on Nigeria's total debt at c. 11% as at September 2022. As at November 2022, actual FGN debt service (NGN5.24trn) gulped the bulk of FGN revenue of NGN6.50trn.

Comparing the underperformance of revenue with the mounting debt service amount has continued to raise concerns about the sustainability of the country's debt position.

### Yet, More Deficit in the 2023 Budget

The 2023 FGN budget contains a planned deficit of NGN11.33trn out of which NGN8.80trn is planned to be funded through new borrowings. The borrowing is expected to be a mix of domestic and external borrowings in the ratio 80:20 respectively, although recent developments indicate that the FGN is averse to external borrowing in 2023. We posit that the new borrowings are likely to come at higher costs given the rising interest rates environment.

As a result of these concerns, Nigeria's credit rating was downgraded by major rating agencies in 2022. Moody's (from B2 to B3) and Fitch (from B to B-) took turns to relegate Nigeria's credit standing to only a notch above the category of poor quality and very high-risk instruments. This implies that investors might price Nigerian-issued debt instruments at a higher yield, leading to higher borrowing costs. Furthermore, another downgrade of Nigeria's credit rating would mean Nigeria's treasury instruments would be judged to be of poor quality.

## Finding the Ways and Means Out of the Strait

A controversial aspect of Nigeria's public debt is the financing of the FGN source from the CBN, popularly called "Ways and Means" (W&M). While this is a legally permissible financing channel for the FGN, there are regulations surrounding the extent to which the CBN can lend to the FGN. The CBN Act permits only a maximum of 5% of FGN's previous year revenue to be sourced from W&M but this has been breached over time. For instance, in 2021, total FGN revenue was c.6.01trn, 5% of which is c. NGN300bn, the maximum legally permissible amount of W&M in 2022. However, the additional borrowing from W&M in 2022 alone (January - October) was NGN6.32trn, which represents c. 105% of 2021 FGN revenue and c. 86% of total 2022 FGN budget deficit.

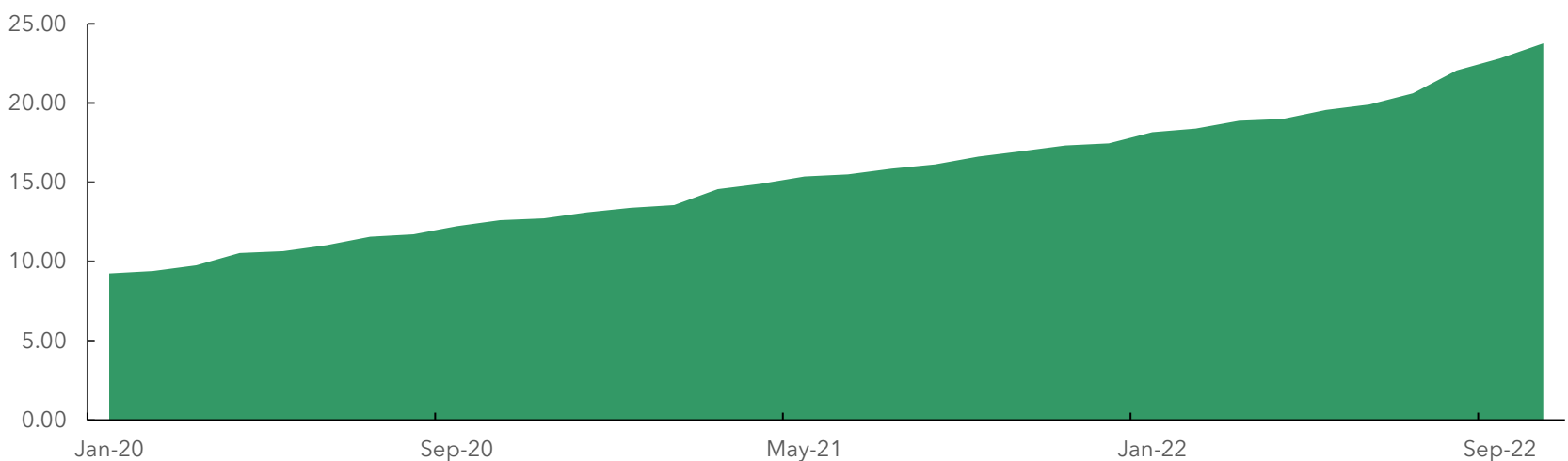
As part of efforts to relieve the FGN of the burden of repayment, the government recently announced a plan to securitize the W&M as a 40year debt at 9% interest rate. Although this plan has suffered a setback as the National Assembly rejected it, getting through with it will bring the W&M into Nigeria's reported debt stock, which would total c. NGN61tr. This will put further pressure on debt servicing and could trigger another credit rating downgrade, especially as there is only an expected marginal improvement to the dwindling revenue signalled from the new Finance Act.

*"It is thus pertinent to find sustainable ways to free up unproductive expenses of the government, particularly petroleum subsidy. This is a major leakage that has continued to affect the federal government in several ways: loss of revenue from the NNPC and higher subsidy payment in the face of a strengthening dollar & higher crude oil prices in the international market. In our view, a total removal of subsidy and additional revenue sources are critical to engendering fiscal sustainability and avoiding another credit downgrade."*

### The Needle's Eye or Another Downgrade?

The continuous spike in W&M has added another bit of concern to Nigeria's debt profile and fiscal sustainability. Notably, Nigeria's reported debt stock excludes the W&M balance.

**Chart 33: Trend of Ways and Means Balance (NGN'tr)**



Source: CBN, Meristem Research.

# External Sector

## External Sector: An Overview

Data suggests that Nigeria's external position remains weaker than the level implied by economic fundamentals (balance of payment and foreign trade data). The Current account and trade balances continues to be supported by the uptick in crude oil prices moderating the otherwise negative effect of higher income repatriation (+44.77% YoY). Moreover, outflows in the financial account from banks and non-banks outpaced the inflows, exerting further downward pressure on the country's external reserve balance.

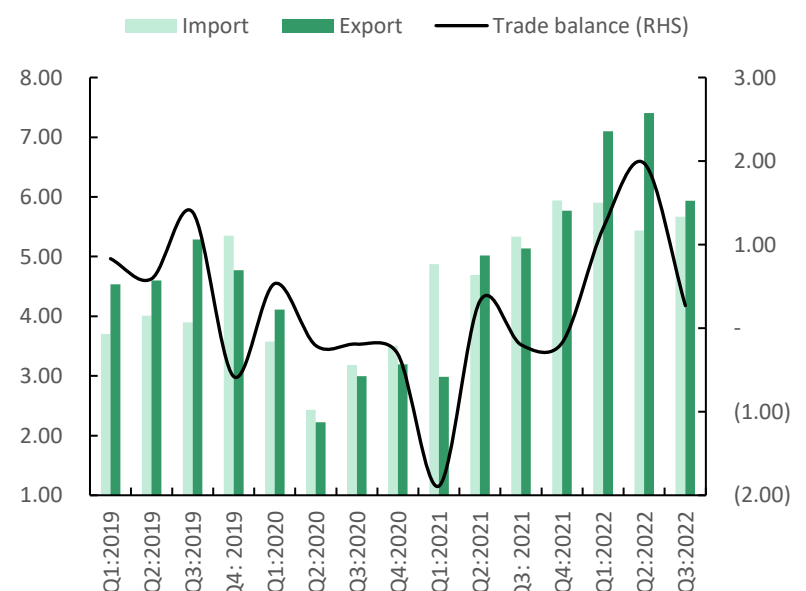
The Current account surplus increased to 4.68% of nominal GDP in Q2:2022 (from -0.42% in 2021 owing to the current account deficit) largely on the back of higher crude oil prices and remittance inflows. In 2023 the surplus is expected to widen even further. While FX illiquidity and unavailability should continue to limit import, the OPEC's commitment to keeping oil prices around current levels should bolster exports.

### Crude Oil Export Underscore External Fundamentals

Against the backdrop of rising crude oil prices and reducing import bill, the current account (CA) balance recorded its 4<sup>th</sup> consecutive quarter of surplus in Q2:2022 (USD5.07bn vs USD2.63bn in Q2:2021), buoyed by the highest crude oil and gas exports since Q3:2014. The latest foreign trade figures published by the National Bureau of Statistic (NBS) for Q3:2022 paints a similar story.

The country recorded a trade surplus (NGN269.34bn) for the third consecutive quarter (albeit slower than Q2:2022 of NGN1.97trn) on the back of gains from higher crude oil prices as oil exports contribute c.79% of total exports. Cumulatively, the trade balance over the nine-month period stood at a surplus of NGN3.44trn (from a deficit of NGN1.76trn in 9M:2021) As a result, the country's terms of trade (price of exports over price of import) also improved to 1.05x (from 0.96x in Q3:2021, respectively). However, the trade surplus (NGN269.34mn or 6.58% of GDP) in the third quarter reversed the post-pandemic trade recovery witnessed in the preceding quarters.

**Chart 34: Nigeria Foreign Trade Statistics**



Source: NBS, Meristem Research.

In our H1:2022 outlook, we highlighted some of the schemes of the CBN to attract remittance inflows into Nigeria, including RT200 and Naira4Dollar scheme. While the monetary authority maintain that the schemes have been significantly attractive, we posit that the impact has been mild due to deteriorating economic conditions from major countries where diaspora inflows have been significant in the past (markedly the U.S.A. and the U.K.). Remittance inflows declined by 0.54% YoY and 5.54% QoQ in Q2:2022, remaining below pandemic levels.

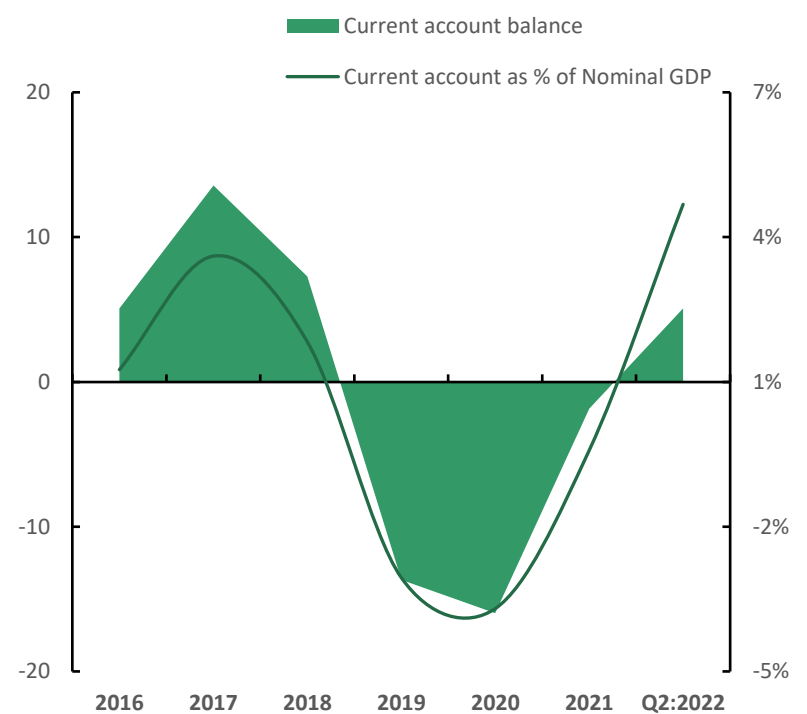
On the other hand, the financial account recorded a net accumulation of financial liabilities (USD3.07bn) largely due to increased inflow from investment in domestic debt instruments, currency swap, and currency deposits by the monetary authority.

We also observed that investments in global debt instruments increased to the highest since Q4:2015.

The NBS's data on capital importation also validates this narrative as Foreign Portfolio Investment (FPI) investments in bonds and money market instruments were significant catalysts for the 75.34%YoY increase in total capital imports.

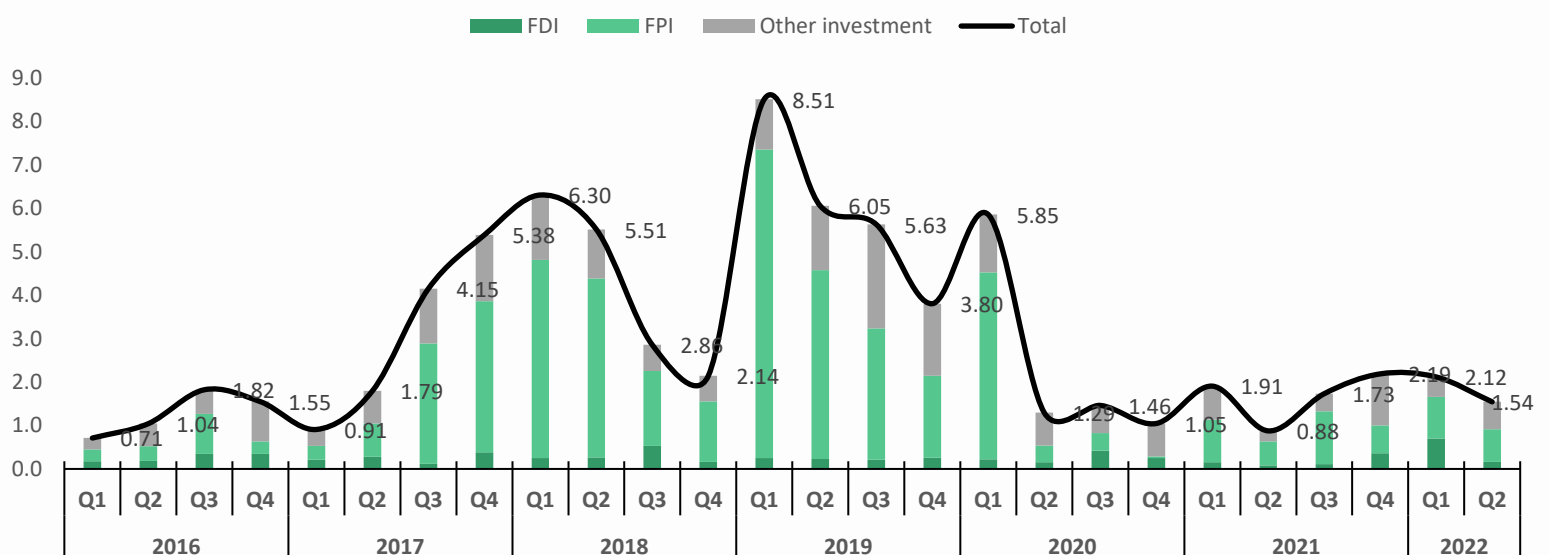
In our view, these all reflect the attractiveness of yields in fixed-income financial markets on the backdrop of a tighter monetary policy stance globally and in the domestic market.

**Chart 35: Current Account Balance as % of GDP**



Source: CBN, World Bank, Meristem Research.

**Chart 36: Quarterly Capital Importation**



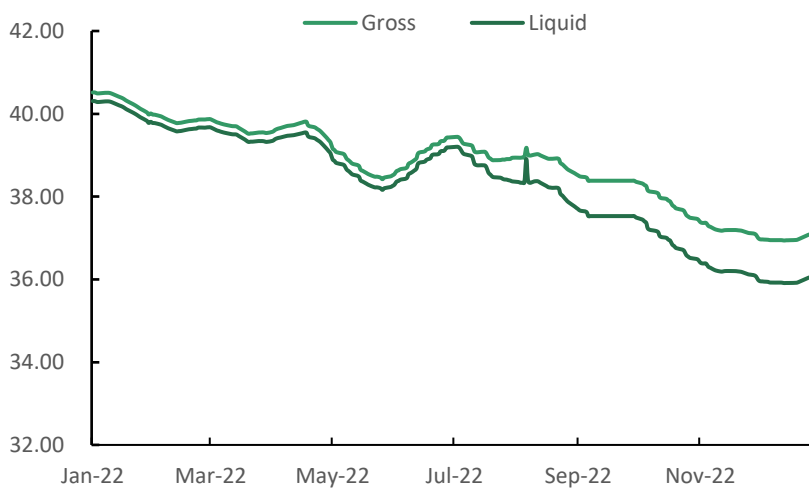
Source: NBS, Meristem Research.

## External Reserves and Exchange Rate:

### Reserve Balance Remain Depressed Despite Impressive Fundamentals

Despite these implied improvements in the balance of payment position, the external reserves continued to decline, impeding the apex bank's ability to defend the currency. The external reserve balance has been on a free fall, declining to USD37.09bn in December 2022 (from USD40.52bn as at the start of the year) as the high petroleum subsidy bill and low accretion from non-oil sources have continue to deplete the FX reserves. The apex bank's interventions in the inter-bank foreign exchange market aimed at enhancing supply also pulls the balance further downward.

**Chart 37: Daily External Reserve balance**



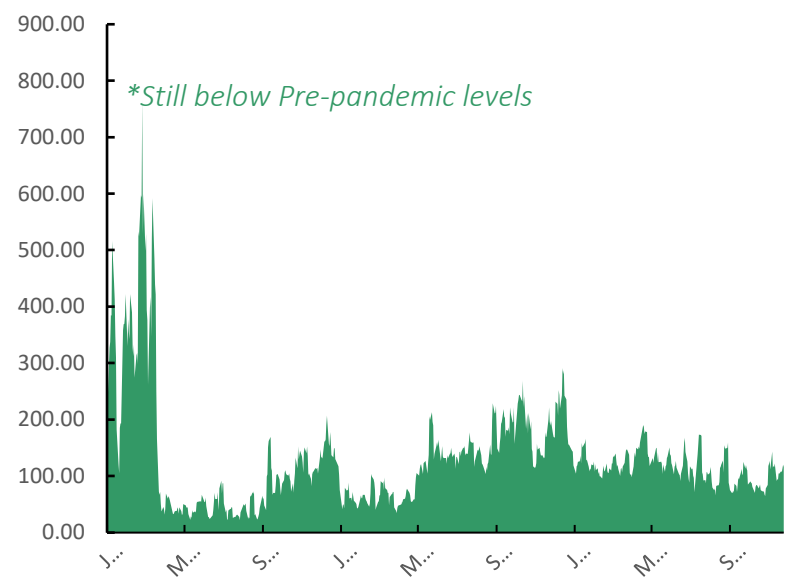
Source: CBN, Meristem Research.

In the foreign exchange market, the official exchange rate of the Naira was relatively stable (depreciating by 7.05% to NGN445.30/USD in 2022), compared to the parallel market (depreciation of c.32% to NGN745.00/USD). Low transaction volumes at the I&E Window, mounting capital repatriation pressures, low FX inflows and its resultant effect on accretion to the external reserves thus provide minimal optimism about the improvement in exchange rate in 2023 (both official and parallel market rate).

In addition, the CBN's contribution at the I&E window has declined significantly below pre-pandemic levels (3-year CAGR of -29.20%), reflecting the apex bank's limited capacity to defend the Naira.

On a positive note, the external reserves remained above the benchmark of 3.0 months of import cover recommended by the IMF standard and could finance up to 9.35 months of import as of August 2022.

**Chart 38: Turnover at I&E Window (5-day Moving Average)**



Source: FMDQ, Meristem Research.

In 2023, we expect these current conditions depressing reserves to remain. The OPEC's commitment to maintaining crude oil prices around current levels provides optimism for the current account. However, low production volumes in the country could limit the surplus. The USD500mn Eurobond re-payment scheduled for July 2023 is also expected to drawdown on the reserves balance. However, the likelihood of Dangote Refinery being operational in Q2:2023 could reduce pressure on the FX reserves although we think that the net effect of the refinery would be minimal. The recently approved IMF Food shock window is also a potential FX source for the reserves balance due to its availability for countries impacted by the global food crisis.

## Naira Devaluation: How Likely?

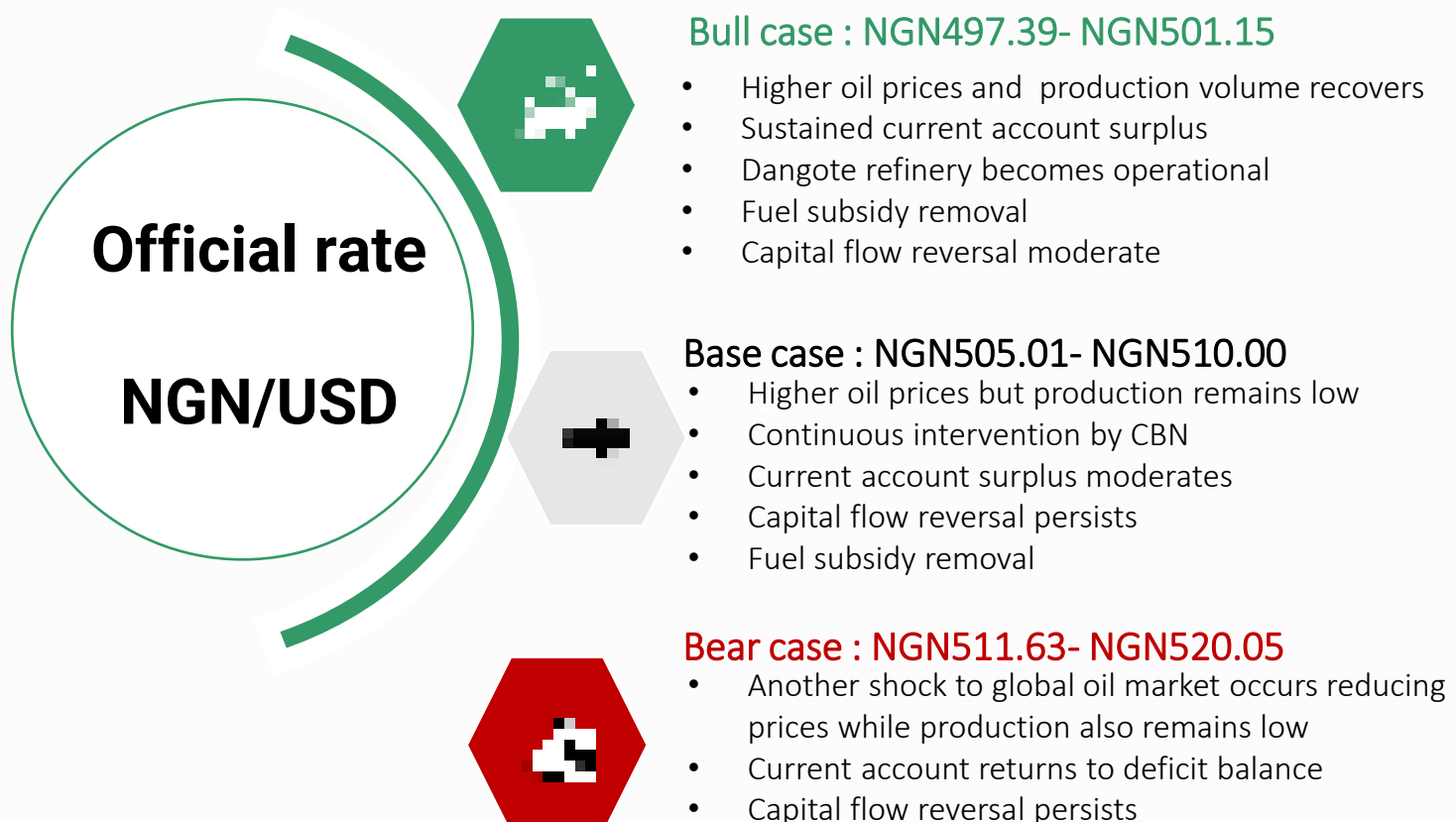
As we opined in our [Macroeconomic commentary](#), we do not rule out the possibility of another Naira devaluation in 2023 to allow the exchange rate to reflect current realities. This opinion is based on two major factors:

Firstly, Non-deliverable Forwards at the Naira settled OTC FX futures market as of December 30<sup>th</sup>, 2022, reveals that contracts maturing in one year closed at NGN529.55/USD. In our view, this reflects investors' pessimism about the direction of the Naira's value against the greenback.

Secondly, considering that the Naira has been devalued in 4 out of the past five years (either at the official or I&E Window), the high likelihood of further strains in FX supply, declining foreign investor confidence in the capital market and other weak macroeconomic variables, signals the possibility of another currency devaluation.

On the other hand, the potential removal of the petroleum subsidy bill would improve accretion into the FX reserves and strengthen the CBN's ability to defend the domestic currency.

## Average exchange rate expectation for 2023



# Politics



## All Eyes on 2023 Elections

As expected, the Nigerian political landscape is currently clouded by the ongoing discussions and assessments of the 2023 general election, especially for the Presidency. While 18 candidates are vying for the Number One Citizen’s spot, the attention has primarily been on three candidates:

- Bola Ahmed Tinubu (All Progressives Congress – APC)
- Atiku Abubakar (Peoples Democratic Party - PDP)
- Peter Obi (Labour Party – LP).

We summarize our analysis of the candidates' past political accomplishments, party ideologies, and manifesto below:

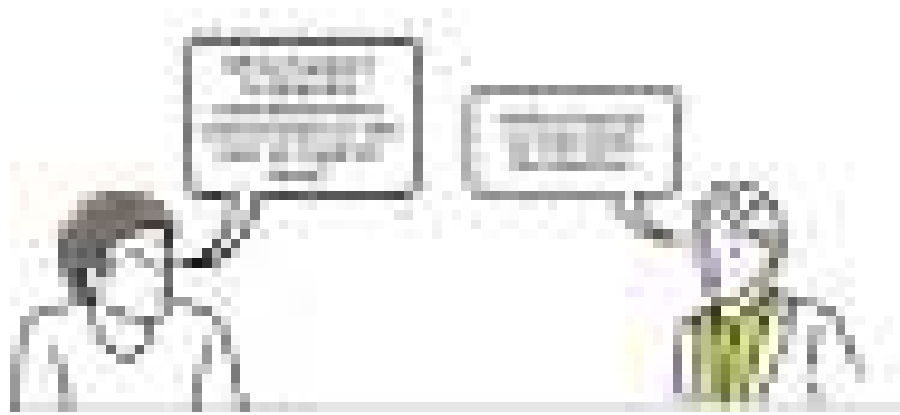
**Table 6: Overview of Front Runners’ Ideology**

Candidates	Major Political Accomplishments	Political Party Ideologies	Proposed Policy Plan
	<ul style="list-style-type: none"> <li>• Digitized tax collection in Lagos</li> <li>• Introduced free health policy for Lagosians below the age of 18 and above 65 years</li> <li>• Established and restructured agencies such as LAWMA, LASTMA, LASAMBUS, RRS, etc.</li> <li>• Created an independent power plant</li> </ul>	<ul style="list-style-type: none"> <li>• National Security</li> <li>• Infrastructure Development</li> <li>• True Federalism</li> </ul>	<ul style="list-style-type: none"> <li>• Growth-oriented fiscal policy</li> <li>• Federalism</li> <li>• Optimization of economic growth through job creation</li> <li>• Fuel subsidy removal</li> </ul>
	<ul style="list-style-type: none"> <li>• Led the economic team that initiated successful reforms in the pensions, banking, and telecommunications sector.</li> <li>• Led the economic team that successfully negotiated a deal to settle Nigeria’s total debt of USD18bn in 2005</li> </ul>	<ul style="list-style-type: none"> <li>• Democracy and Social Justice</li> <li>• Private-sector led economic development</li> </ul>	<ul style="list-style-type: none"> <li>• Restructuring and True Federalism</li> <li>• Private sector-led economic development</li> </ul>
	<ul style="list-style-type: none"> <li>• Initiated Sub-Sovereign Wealth savings (Pioneer in Nigeria)</li> <li>• Established the first public teaching hospital in Anambra</li> <li>• Introduced Anambra Integrated Development Strategy – a development model</li> </ul>	<ul style="list-style-type: none"> <li>• Social Democracy</li> <li>• Public and Private sector-led economic development</li> </ul>	<ul style="list-style-type: none"> <li>• National Unity</li> <li>• Production-centred and export-oriented economy</li> <li>• Public-Private partnerships</li> <li>• Subsidies Removal</li> </ul>

## Who is likely to be Nigeria’s Next President?

Given that it would likely have a considerable impact on their 2023 investment decisions, it is understandable that internal and external stakeholders are concerned about the incoming president in 2023.

In order to determine the likely winner of the upcoming Presidential election, we considered polls from two reputable and well-known research companies, NexTier Advisory and Fitch Solutions.



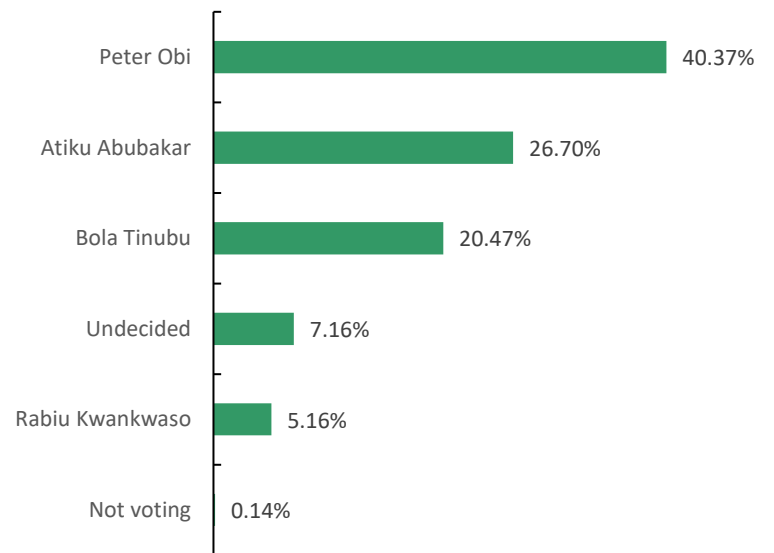
*"In NexTier's survey, polls were conducted in twelve states (two states per geopolitical zone) which included 2,000 registered voters in rural committees (with focus was on local governments without tertiary institutions). According to the survey results, 807 respondents (40.37%) favored the LP's candidate - Peter Obi - in the upcoming election. Peter Obi also had the highest level of preference across all age categories."*

In another survey by Fitch Solutions on the likely winner of the 2023 Presidential election, Peter Obi had the highest votes. However, the research institution maintains that the polls exaggerate the support for Peter Obi – considering that most of his supporters are young and active on social media. Thus, the research agency highlighted that Bola Ahmed Tinubu has the highest chance to win the 2023 Presidential election based on the following reasons:

- Incumbency benefits for Bola Ahmed Tinubu
- Peter Obi's lack of support in the Northern part of Nigeria
- Labour Party's limited structure and popularity in the North

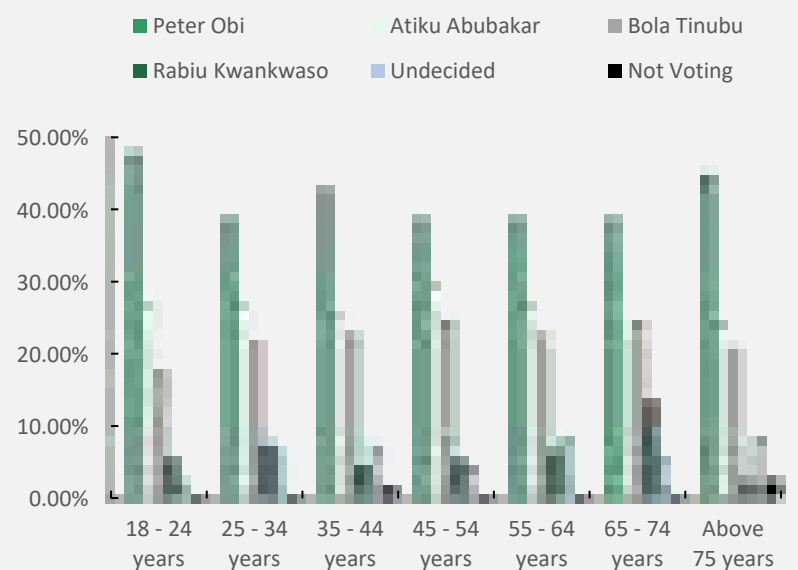
*"In our view, the election will be keenly contested for by the three candidates. Additionally, while each candidate has their main regions of strength, we opine that they are evenly capable of winning at least one-quarter of the votes in two-thirds of Nigeria's 36 states."*

**Chart 39: Respondents' Votes**



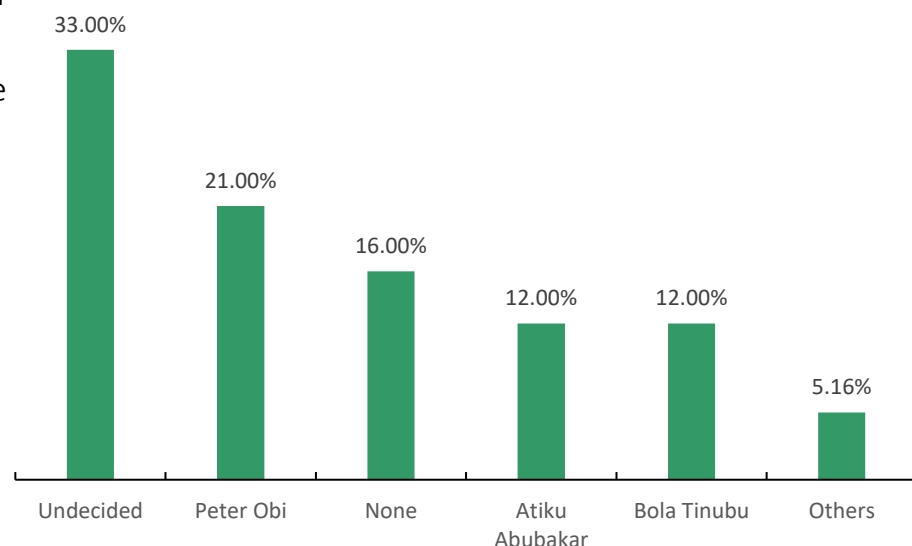
Source: NexTier, Meristem Research

**Chart 40: Respondents' votes (Age preferences)**



Source: NexTier, Meristem Research

**Chart 41: Peter Obi Leads Fitch Solutions' Poll**



Source: Fitch Solutions, Meristem Research

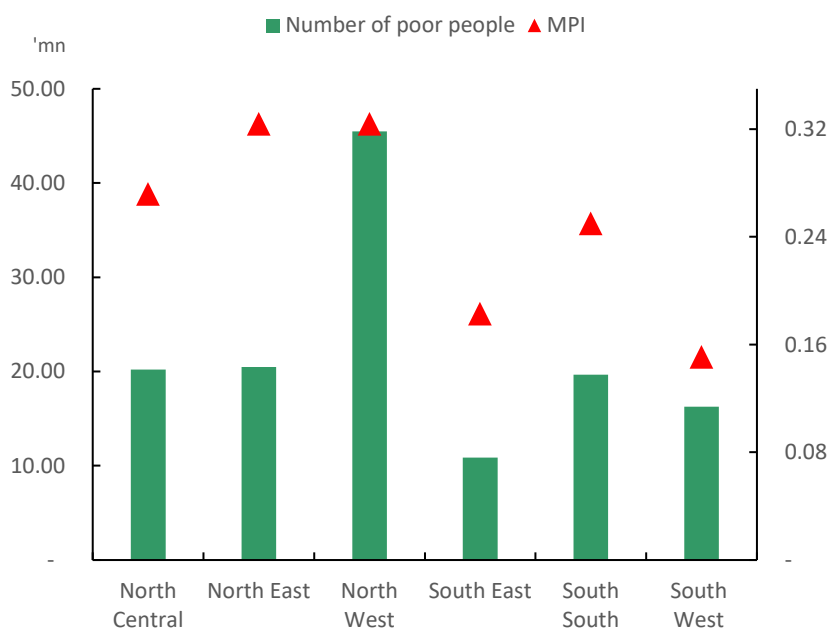
# Socio-Economic Development

## Widespread Poverty in Nigeria

According to the World Bank, nearly 4 in 10 Nigerians live below the poverty line even before the COVID-19 pandemic. Also, findings from the 2022 Nigeria Multidimensional Poverty Index (MPI) Report by the National Bureau of Statistics (NBS) indicate that over half of Nigeria's population (133 million people) is multidimensionally poor. This is corroborated by an estimation by World Poverty Clock (WPC) which postulate that one out of every three Nigerians is multidimensionally poor.

The NBS considered four significant dimensions for the survey: education; health; living standards; and work and shocks. Nigeria's MPI was estimated to be 0.257 – which signifies that the poor populace suffers over one-quarter of the likely deprivations. The major deprivations are cooking fuel, sanitation, healthcare, food insecurity and housing. Further analysis of the report revealed that more people (72%) living in rural areas are poor than those living in urban areas (42%). In our [Nigeria MPI Report Flash](#), we gave more insights on the 2022 Nigeria MPI report

**Chart 42: Multidimensional Poverty by Geopolitical Zone**



Source: NBS, Meristem Research

## Migration Trend:

### Red Light, Green Light

Like other climes, Nigeria has been rocked with massive migration issues. In recent times, there has been a notable increase in Nigerians migrating to other countries since the resumption of visa approvals following the relaxation of Covid-19 related restrictions. The quest for greener pastures, dissatisfaction with the country's current economic situation, insecurity, and educational pursuits are some of the reasons for the mass migration. However, while relocation is an inherent trait of human nature, mass human capital export creates a brain-drain vacuum in several sectors of the Nigerian economy.

According to the Home Office in the UK, the number of visas issued to Nigerians between January to September 2022 was 178,908 – *the highest in Africa* (vs 106,609 and 54,975 in 2021FY and 2020FY, respectively). Similarly, relative to other nationalities, Nigeria had the highest increase in approved study visas as of September 2022 compared to 2021FY.

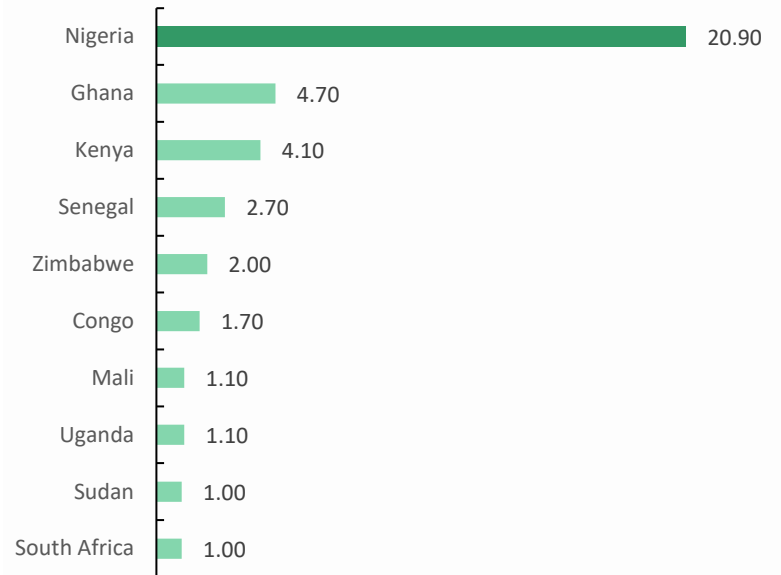
**Chart 43: Nigerians’ Issued Visas to the UK**



Source: Home Office, Meristem Research

The most significant implication of this trend is the likely widening gap in the human capital and expertise required in the sectors of the economy. On the bright side, the migration has continued to support remittances into Nigeria. According to the World Bank, in 2022, Nigeria was the top recipient of diaspora remittances in the Sub-Saharan Africa region. However, the expected growth of remittance inflow for 2022 is 7.50%, lower than the 13.20% growth witnessed in 2021FY. This falloff can be attributed to macroeconomic challenges in regions where remittances have been significant in the past ( including the U.S.A., the U.K., and the Euro Area). Furthermore, it is projected that the likelihood of recession which could further moderate the real wages in these countries would prompt a further slowdown in the growth of remittance flows to 4.50% in 2023.

**Chart 44: Nigeria was the Largest Remittance Recipient in SSA for 2022 (USD’bn)**



Source: World Bank, KNOMAD, Meristem Research

# Trading is no longer a chore

What you know the Merittrade App

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# Domestic Equities

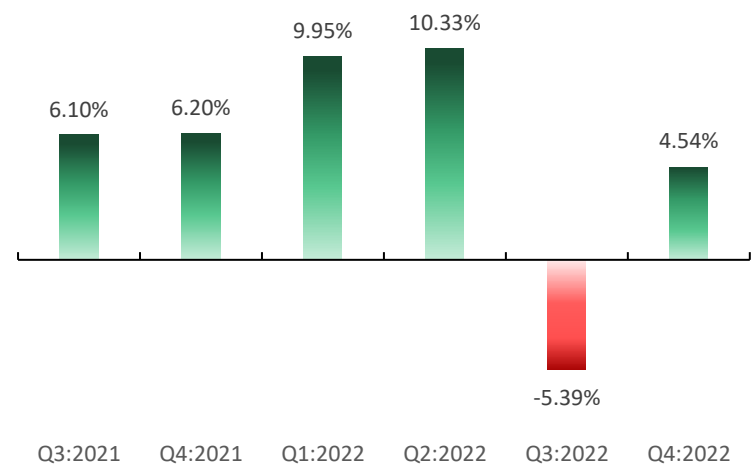
## Two Converse Halves on the Local Bourse

As we mentioned in our H2:2022 outlook, the Nigerian equities market bucked global trend to deliver an impressive first-half performance. The NGX-ASI peaked at 54,085.30pts in May and closed H1:2022 with a return of 21.31%.

Contrarily, the market was predominantly bearish in H2:2022 (before the bulls returned to the market in November). The shift in policy stance by the Monetary Policy Committee since its meeting in May, (*which signalled an increase in risk-free rates leading to higher cost of equity*) caused a downturn in equities valuation. Consequently, the market recorded a negative quarterly return (-5.39% QoQ) in Q3:2022 (for the first time in five quarters).

While stock prices remained considerably low in H2:2022, the elevated market risk premium was a factor most investors could not ignore. This fuelled investor’s passivity, despite the seemingly attractive prices. The heightened market risk reflects the skyrocketing inflation, decelerating economic growth, declining external reserve, foreign exchange illiquidity and increased political tension.

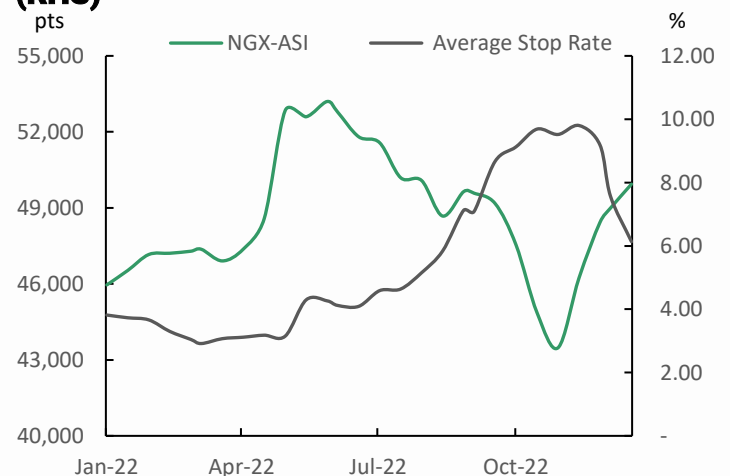
**Chart 45: NGX-ASI Quarterly Returns**



*Source: NGX, Meristem Research*

Together with the dip in equities prices was a concurrent dip in activity level in the market – volume, and number of deals and market turnover declined by 43.98% QoQ, 25.42% QoQ and 43.28% QoQ respectively in Q3:2022 (representing the lowest quarterly activity level in the market since Q2:2021).

**Chart 46: NGX-ASI Trend vs. T-bills PMA Rates (RHS)**

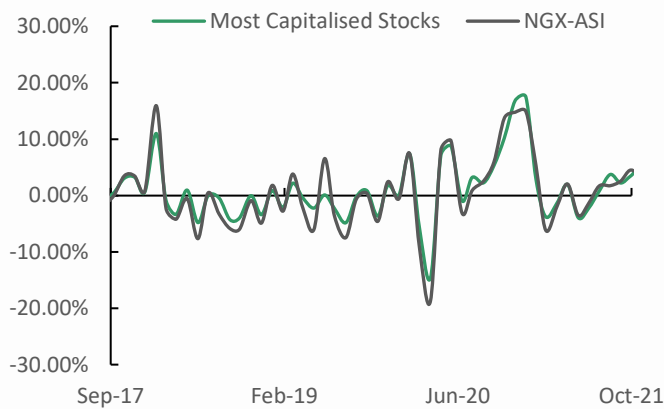


*Source: NGX, CBN, Meristem Research*

### Bellwethers Call the Shot

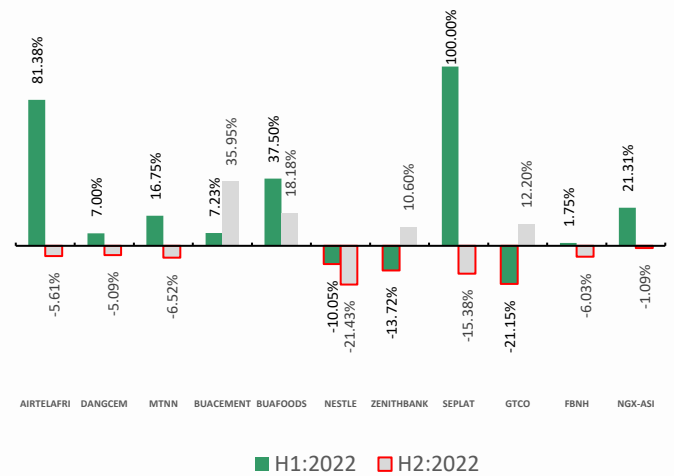
In the past, the broad market index has closely mirrored the performance of the most capitalized stocks on the exchange. For context, the top 10 capitalized stocks presently make up over 80% of the total market capitalization (with an average of 78.07% in the past five years). Unsurprisingly, the performance of the market in 2022 reflected the activities of these heavyweights, as the market return in both H1:2022 (+21.31%) and H2:2022 (-1.09%) neared the weighted average return of the top 10 most capitalized stocks – H1:2022 (+24.64%), H2:2022 (0.74%).

**Chart 47: Correlation of Top Capitalised Stocks and ASI**



Source: Bloomberg, Meristem Research

**Chart 48: Performance of Top Capitalized stocks**

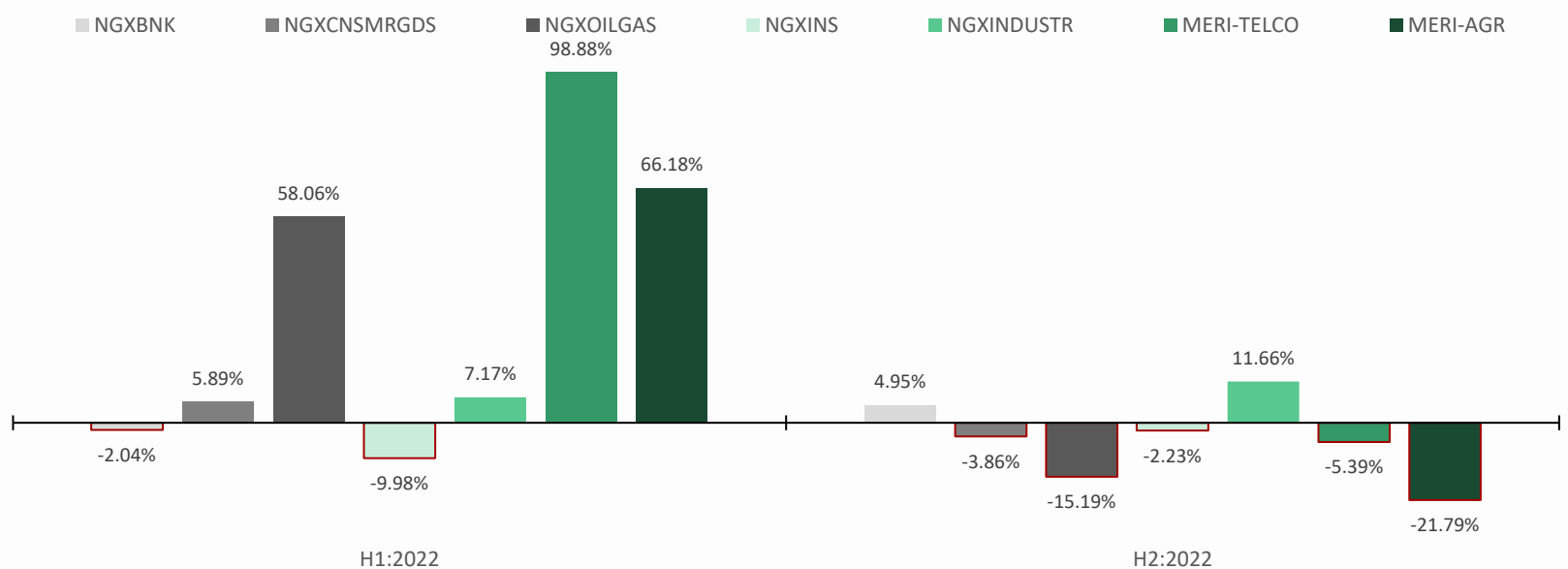


Source: Bloomberg, Meristem Research

### Sectoral Performance

A reflection of the bullish sentiment in the equities market in H1:2022 was a positive outing for all sectoral indices under our coverage. Notably, at least four of the seven sectoral indices we track recorded positive returns during the first two quarters of the year. On the flip side, the bearish sentiment in H2:2022 was also broad-based, as the banking and industrial goods sectors were the only sectors to record gains in H2:2022.

**Chart 49: Sectoral Returns**



Source: NGX, Bloomberg, Meristem Research

### Corporate Actions Skewed to the First Half

Another notable driver of the positive sentiment in the market in H1:2022 was corporate actions, which were well-received by the investing public. Companies' announcements of corporate actions in H1:2022 were broad base across sectors, with the most notable from **DANGCEM**, **BUAFOODS**, **SEPLAT**, **ACCESSCORP**, and **WEMA**.

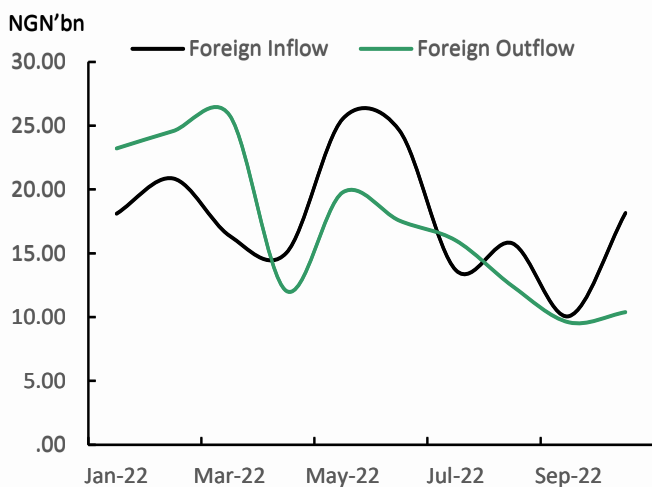
On the contrary, H2:2022 was marked with fewer corporate actions, with the only remarkable corporate actions being – the listing of Geregu Power Plc. shares, **ACCESSCORP**'s acquisition of majority shareholding in Finibanco Angola S.A. and Sigma Pensions Ltd and **FBNH**'s acquisition of Access Pension Custodian Limited. Other corporate actions which were announced during the period but are yet to be conducted are – the third tranche of **DANGCEM**'s share buyback (which is expected to be conducted in January 2023 following Management's guidance) and Purple Real Estate's IPO.

### Foreign Participation Down the Hill

Unsurprisingly, foreign participation in the Nigerian equities market remained abysmally low (albeit higher than the comparable period of last year), as foreign portfolio investors continue to price in higher risk premium in addition to the higher yield opportunity in the developed markets. This made the Nigerian bourse less attractive relative to developed markets fixed income investments. Foreign participation on Custom street (between January and November) totalled NGN364.02bn (vs. 399.18bn in the first 11 months of 2021). Also, the bulk of foreign transactions in the market was during the first half of the year (average monthly foreign transactions in H1:2022 - NGN20.09bn vs. NGN13.32bn in H2:2022).

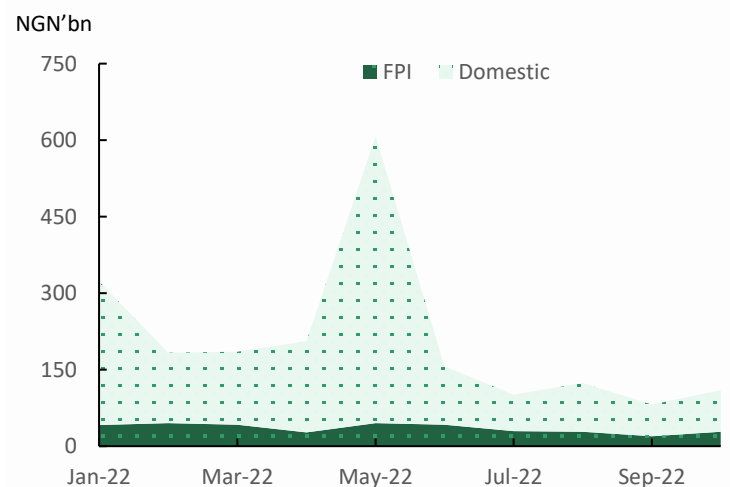
While domestic players remain dominant on the local bourse, their contribution to total activities declined in H2:2022 (domestic players accounted for an average of 76.83% of total market activities in H2:2022 vs. 82.02% in H1:2022). This was due to the faster decline in activities of domestic investors relative to foreign investors.

**Chart 50: Foreign inflow vs Foreign Outflows**



Source: NGX, CBN, Meristem Research

**Chart 51: FPI vs Domestic Players**



Source: NGX, CBN, Meristem Research

## NASD NSI:

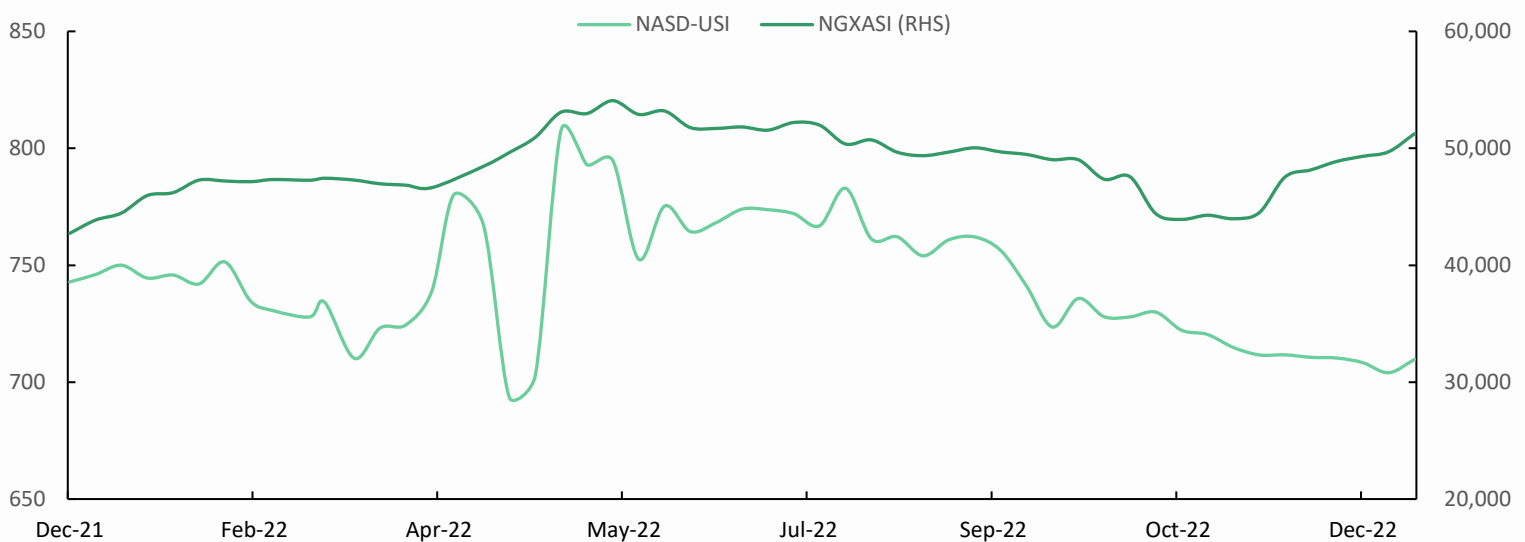
### Treading the Same Path with Customs Street?

In the 2022 fiscal year, the NASD Unlisted Security Index (NASD-USI) and the NGXASI showed some similar trends. Both indexes increased in H1:2022, then began to trend downwards as the Monetary Policy Rate increased. However, there has been a divergence in their performances, owing to sustained bearish sentiments on the NASD-USI while the NGXASI recovered.

Poor corporate governance and the untimeliness of financial reports on listed companies might have worsened investors' sentiments on the NASD-USI. According to the NASD OTC securities categorisation schedule, twenty-eight out of the forty listed companies on the exchange failed to fully comply with the disclosure of financial reporting and publications in the first half of 2022.

On a positive note, the exchange moved forward with its new digital securities platform (N-DSP) initiative with the launch of a digital asset certification program. The N-DSP will enable issuers to tokenize their securities as well as connect with brokers and investors efficiently. While the digital asset certificate which is to be deployed in early 2023 will be required for licensed financial institution to engage in blockchain based digital assets on the platform. **Overall, the NASD-USI declined by 4.47% YtD to settle at 709.66pts.**

**Chart 52: NASD-USI 2022 Trend**



Source: NASD, Meristem Research

## Outlook:

### Risk Premium to Remain Elevated

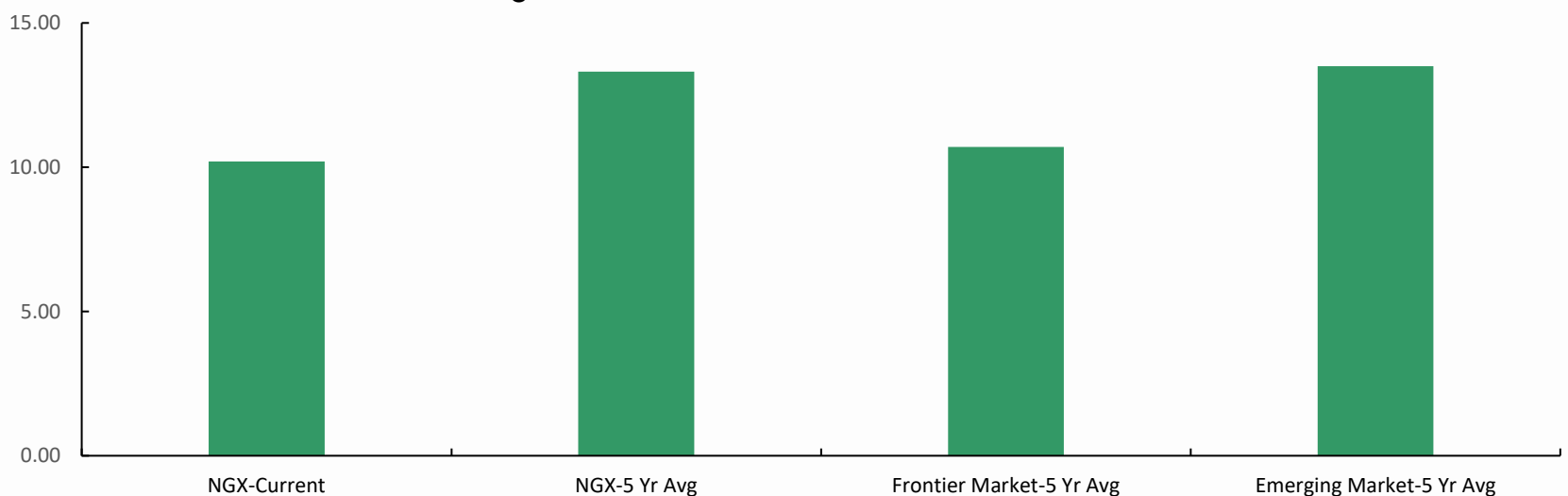
We note the likelihood of a market rally in January, especially due to the optimism that usually comes with the new year, portfolio rebalancing activities, and possible corporate actions like DANGCEM’s buy-back. However, we expect this to be short-lived, as investors move to the less risky fixed-income investments, due to attractive rates and heightened political and economic risks. In our view, the mood in the market post-election will be largely dependent on the ease of transition of power, investors’ confidence in whoever emerges at the polls, and immediate policy decisions.

### Local Bourse Attractive Amongst Key Peers

The Nigerian equities market presently trades at a price-to-earnings ratio of 10.2x, which is a discount relative to its five-year average of 13.31x, emerging markets P.E. of 10.7x, and developed markets P.E. of 13.5x. This suggests an undervalued market and makes a case for investors who are willing to take on the associated risk. Thus, we expect the low valuation to serve as an incentive for highly risk-tolerant investors to channel funds into the equities market in 2023.

We expect corporate performance to remain broadly positive in 2023, with equally impressive dividend declarations. The major downside risk to this is the inflation-driven surge in input costs and less favourable funding conditions which could incentivize firms to retain more income for investment purposes rather than distributing them in the form of cash dividends. Furthermore, we note the increased likelihood of certain corporates that require long-term funding to tend towards equity capital raise (like rights issue) due to the high cost of bonds.

Chart 53: Market Price to Earnings Ratio



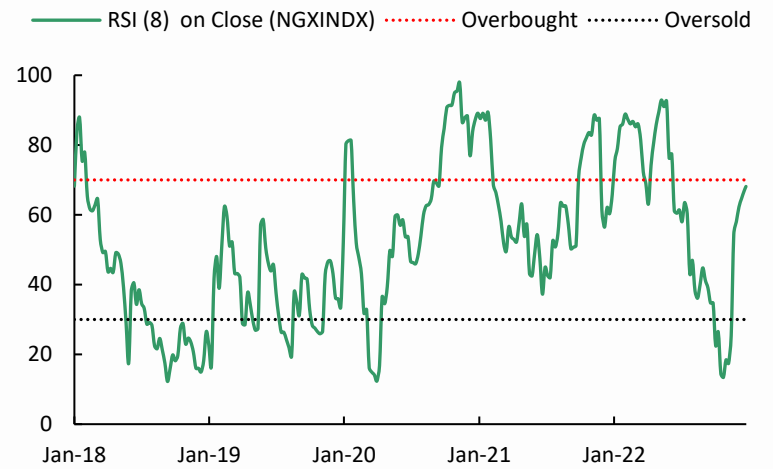
Source: Bloomberg, Meristem Research

### Budding Momentum Ahead of Election

In our 2022 annual outlook, we highlighted the triple top bearish reversal signal and noted the failure of the last two attempts to break above the resistance level (43,387.73pts). The market broke above the resistance level in January 2022 and successfully tested it in November, the level acted as a support for the market rebound.

In the current market phase, technical indicators shows the strength of momentum on the equities market. Also, the next resistance zone is around 54,290.84pts, this implies that there is still some upside to the trend. However, the election is just around the corner and it may trigger some downside risks especially as the technical indicators flashes caution.

**Chart 54: Trend in 8-week Relative Strength Index**



Source: Bloomberg, Meristem Research

## Domestic Equities Outlook:

### Fundamental Approach

Using the fundamental approach, our expected market return for 2023FY was calculated using the 2023FY target prices of our coverage stocks.

**Table 7: Expected Sectoral Returns**

Sector	Weight	Expected Return	Weighted Return
Banking	13.15%	17.01%	2.24%
Insurance	0.41%	8.42%	0.03%
Materials and Industrials	30.73%	2.63%	0.81%
Consumer Staples and Consumer Discretionary	11.56%	12.43%	1.44%
Agricultural Products	1.12%	20.52%	0.23%
Energy	2.90%	8.42%	0.24%
Healthcare	0.14%	52.57%	0.08%
Information Technology	39.62%	11.22%	4.45%
Other Financial Services	0.36%	19.38%	0.07%
<b>TOTAL</b>	100.00%		
<b>Expected Return</b>			9.58%

### Econometrics Approach

In recent years, statistical models, such as the ARIMA model, have been widely used for stock market indices forecasting. Here, we use an ARIMA model to obtain a forecast of the NGXASI using daily data on the All-share index. The popularity of the ARIMA model is due to its inherent properties which reduces the effect of seasonality in stocks market variables and its capacity to model the random noise in the data.

Based on this model, we expect the All-share index to settle at 57,106.94pts, implying a return of +11.43% by 2023FY from close of 30th December 2022.

**Table 8: Weighted Market Return**

Approach	Weight	Returns	Weighted Return
Fundamental approach	50%	9.58%	4.79%
Econometrics approach	50%	11.43%	5.71%
<b>Expected market return</b>			10.50%

# Agriculture

## Macroeconomic Headwinds to Weigh on Growth

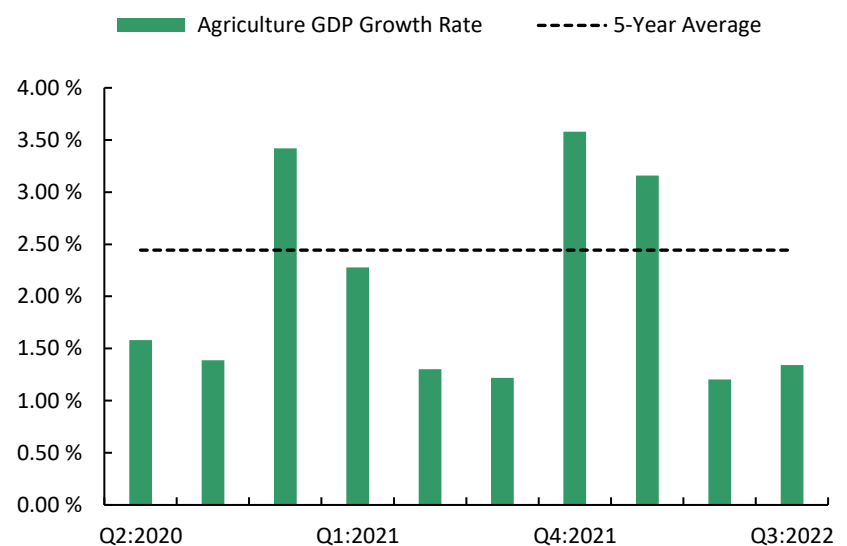
The agricultural sector GDP grew by 1.34% in Q3:2022, albeit at a slower pace relative to its 5-year average of 2.45%. This performance mirrors the challenges which continue to plague the sector such as: the lingering insecurity challenge in the agricultural hubs, poor logistics and storage facilities, inadequate financing for farmers, fractional land ownership, amongst others. In addition, the recent flooding in the economy which ravaged about 33 states (including the food producing regions) and over 700,000 hectares of farmlands, as estimated by the National Emergency Management Authority (NEMA) led to post-harvest losses.

In its regular fashion, the fiscal authority's stance on the sector remains pro-growth, introducing additional intervention policies in 2022. The Federal Government in conjunction with the African Development Bank, International Fund for Agricultural Development, Islamic Development Banks, State Governments and Private Investors launched the Special Agro-Processing Zones Programme in 8 states (Kaduna, Kano, Kwara, Oyo, Ogun, Imo, Cross River, and the Federal Capital Territory).

The programme aims to bring basic infrastructure to rural areas, link smallholder farmers and SMEs in priority value chains. Also, in October 2022, the Federal Government granted incentives that include a 5-year tax and duty-free holidays for agricultural production and processing, zero-tariff rates on the importation of agrochemicals, and tax-free agrarian loans with a moratorium period of over 18 months.

.While these policies will continually provide funding for the sector, other existing structural challenges are expected to continue to limit their impact on the sector.

**Chart 55: Agriculture Sector GDP Growth Rate**



Source: National Bureau of Statistics (NBS), Meristem Research

*“For 2023, we expect the intervention programmes to continue to support the sector. However, the tightening stance of the monetary authorities, the reversal of interest on intervention programmes to 9% from 5%, as well as other structural challenges pose downside risks to this outlook.”*

## Oil Palm Millers: Increased Oil Palm Demand to Bolster Revenue and Earnings Growth

In contrast to H1:2022 where global CPO prices rallied, increased CPO supply from the largest oil palm producers (Indonesia and Malaysia), as well as decreased demand from Asia (the largest consumer of oil palm globally) resulted to a decline in global CPO prices in Q3:2022. According to the World Bank Commodity Price Data, global oil palm price declined by 11.69% YoY in Q3:2022. Given that global CPO prices serve as a benchmark for domestic prices, the domestic oil palm players recorded a decline in revenue in Q3:2022 (**OKOMUOIL** : -53.52% QoQ; **PRESCO** : -20.81% QoQ). This coupled with increased costs of fertilizers as well as rising energy prices dampened their earnings. Hence, **OKOMUOIL** and **PRESCO**'s earnings in Q3:2022 tapered by 83.47% YoY and 68.32% YoY, respectively.

*"In 2023, we expect the moderation in global oil palm prices to persist due to increased Crude Palm Oil (CPO) supply to the global market. Hence, we anticipate slower prices on the domestic scene. However, we expect increased demand from the growing population for cooking and packaged foods to bolster the revenue and earnings of the domestic players."*

## Feed Millers: Cost Pressures to Drag Earnings

Rising costs of wheat and maize (the major inputs for animal feeds) exacerbated by the lingering Eastern-Europe crisis has continued to exert pressure on the production costs incurred by the domestic feed millers. According to the World Bank Commodity Price Data, global prices of wheat and maize in Q3:2022 increased by 11.39% YoY and 16.01% YoY. In addition, the insecurity challenge in the Northern region where the inputs are mainly produced have continued to adversely affect their supplies domestically thereby driving their prices up.

Consequently, as of November 2022, domestic wheat and maize prices reported by Selected Food Price Watch expanded by c.16% and c.25%, respectively. This, coupled with the prevailing headwinds in the economy has adversely impacted the cost of production. As a result, **LIVESTOCK**'s cost to sales ratio deteriorated to 92.30% in 9M:2022 (vs. 89.20% In 9M:2021). This, coupled with the increase in finance cost by +169.07% YoY in 9M:2022 led to a decline in earnings by 145.47% YoY.

*"In 2023, while increased demand for animal feeds is anticipated to continue to support revenue, supply glut of the key inputs is expected to linger due to the global supply chain disruptions. Also, the heightened inflationary environment as well as foreign exchange volatility are projected to exert pressure on the production costs, thereby dragging earnings."*

### Valuation and Fundamental Metrics

	Fundamentals					Trailing				Valuation						
	AT	NM	ROE	ROA	Lev	EPS	BVP	P/E	P/BV	Exp Div Yield	Target PE	Exp. EPS	2023 TP	CP	UPP	RT
<b>OKOMUOIL</b>	0.78	38%	56%	29%	1.93	22.37	39.62	7.38x	4.16x	6.06%	9.40	20.42	191.92	165.00	+16%	BUY
<b>PRESCO</b>	0.51	32%	59%	16%	3.67	23.05	39.06	5.97x	3.52x	5.82%	7.22	23.87	172.25	137.50	+25%	BUY

# Banking

2022 can be considered a relatively unsettling year for the Nigerian banking sector as banks faced a stern regulatory hurdle amid a challenging macroeconomic environment. Broadly, these factors influenced the banks' financial performance, and rubbed off on the market returns of the stocks. Nevertheless, Nigerian banks were resilient as they sought improved means to record solid financial performances. Below is a review of the recent developments in the sector during the year and their implications on financial performance.

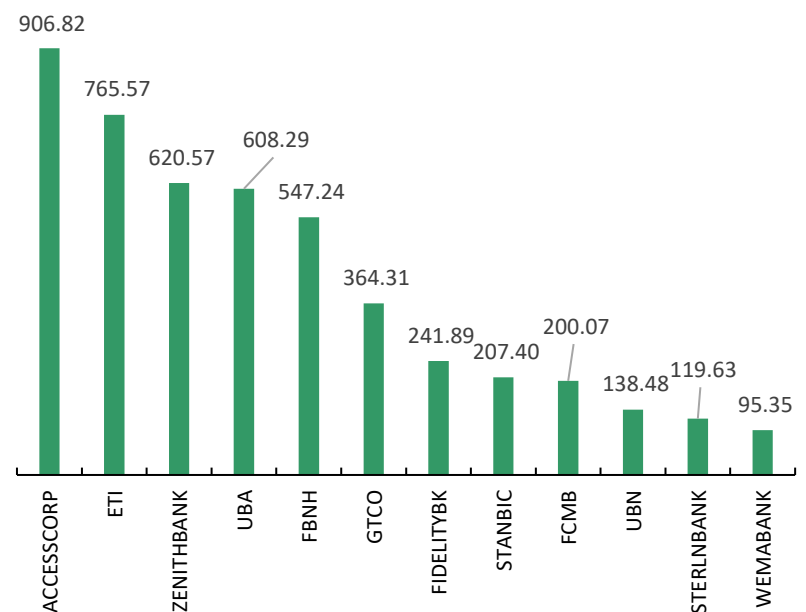
## Higher Lending Rates Drive Topline Growth

In 2022, Nigerian banks primarily benefitted from the consecutive Monetary Policy Rate (MPR) hikes. Particularly, the higher MPR encouraged the banks to reprice their loans, as indicated by the higher average prime and maximum lending rates (which rose by 149bps and 49bps to 13.17% and 28.14%), respectively. Also, the 500bps increase in MPR pushed yields on investment securities upwards. Cumulatively, these factors drove the banks' interest income upward.

In addition, Nigerian lenders broadly recorded growth in non-interest income, mainly driven by higher trading income, more digital transaction volume and fees, the consolidation of non-banking subsidiaries, and increased foreign exchange revaluation gains (due to the depreciation of the Naira). For our coverage banks, only **UBN** (-33.22% YoY) and **FIDELITYBK** (-14.62% YoY) recorded a decline in their nonfunded income in 9M:2022. This was primarily caused by lower recoveries and foreign exchange revaluation gains, respectively.

Remarkably, **ACCESSCORP** reported the highest annual increase in non-interest income (155.84% YoY). This is explained by the expansion of the group's non-banking service offerings. Consequently, our coverage banks' gross earnings improved by 23.27% YoY to NGN4.82trn in 9M:2022 (vs NGN3.91trn 9M:2021).

**Chart 56: 9M:2022 Gross Earnings of Coverage Banks (NGN'bn)**



Source: Companies' Financials, Meristem Research

*"In 2023, we expect lending rates to remain elevated, on the back of our outlook for a higher MPR. Similarly, investment yield will be higher, both leading to increase in funded income. For non-funded income, we project that the recent CBN's Naira redesign policies should lead to increased digital transaction volume. Also, our expectation of further depreciation of Naira could boost the banks' foreign exchange revaluation gains. Overall, we project an increase in the gross earnings of our coverage banks in 2023".*

## Weakening Macroeconomic Environment Increases Banks' Loan Loss Provisions

Like other sectors in the country, the Nigerian banking sector was affected by the country's macroeconomic headwinds both directly and indirectly. Notably, the high loan exposure to key sectors (oil and gas, manufacturing, trade, and agriculture) most susceptible to macroeconomic shocks informed higher loan loss provisions given the higher risk of default. Hence, our coverage banks' impairment charges jumped by 32.07% YoY to NGN240.25bn in 9M:2022.

*In our view, the banks' exposure to these sectors is not likely to reduce as they are considered pivotal to the economy's economic growth. Thus, in 2023FY, we project a further increase in our coverage banks' loan loss provisions as the business environment is likely to remain challenging. However, the implementation of the Global Standing Instruction (GSI) which commenced earlier in 2022 will be helpful in limiting risk exposures.*

## Increased Quest for Non-Banking Subsidiaries

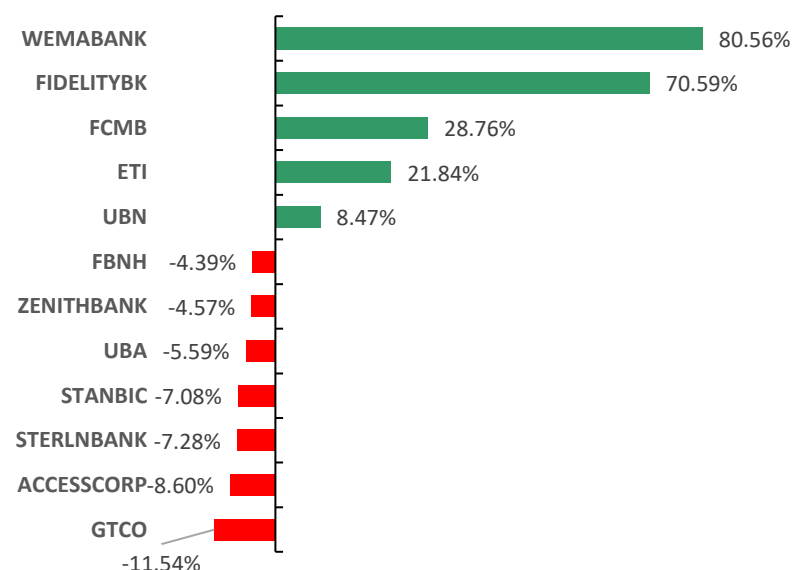
In 2022, the Nigerian banking space witnessed significant corporate actions, most of which revolved around establishing and/or acquiring non-banking subsidiaries. Notably, the revival of the universal banking license paved the way for some banks to grow organically and inorganically across non-banking financial services. Further to that is the increasing acquisition of subsidiaries outside Nigeria. Access Holdings Plc. (**ACCESSCORP**), Guaranty Trust Company Holding Plc. (**GTCO**), Stanbic IBTC Holdings Plc. (**STANBIC**), FBN Holdings Plc (**FBNH**), and Fidelity Bank Plc. (**FIDELITYBK**) are noteworthy banks that stirred the wheel of these activities.

Recently, we published a [note](#) where we analyzed the dynamics and implications of the corporate actions in 2022.

## Resilient Share Performance Amid Mixed Investors' Sentiment

The banking sector - the third best-performing sectoral index – ended 2022 in the positive zone, albeit marginally at +2.81%. Within the year, however, the dynamics of the broad equity market rubbed off on banking tickers. The selloffs on the tickers peaked in July when the banking index plummeted to its year low of 354.79pts. Similarly, there were further selloffs in October, when most tickers, including some of the Tier-1 banks – **UBA** (NGN6.55), **GTCO** (NGN16.85), and **ACCESSCORP** (NGN7.50) – reached their year lows. The bargain hunting opportunity presented at that level attracted investors' interest. As a result, in Q4:2022, the **NGXBNK10** gained 10.10%. Notwithstanding, the banking sector index remains the most undervalued sectoral index, at a P/E ratio of 2.60x.

**Chart 57: 2022 Share Price Performance of Banking Tickers**



Source: Bloomberg, Meristem Research

**Table 9: Our Outlook for Key Banking Sector Metrics in 2023**

Key Metric	Upside Factors	Downside Risks	Outlook
<b>Earnings</b>	<ul style="list-style-type: none"> <li>Increase in asset yield</li> <li>Higher loan volume</li> <li>Higher digital transaction volume</li> </ul>	<ul style="list-style-type: none"> <li>Higher cost of funding</li> <li>Limited credit creation capacity</li> <li>Higher operating costs</li> </ul>	Stable
<b>Asset Quality</b>	<ul style="list-style-type: none"> <li>Promotion of Global Standing Instruction</li> <li>Existence of Special Tribunal for loan recovery</li> </ul>	<ul style="list-style-type: none"> <li>Slowdown in economic activities</li> <li>Deteriorating macroeconomic conditions</li> </ul>	Moderate
<b>Capital Adequacy</b>	<ul style="list-style-type: none"> <li>Recapitalization of earnings</li> </ul>	<ul style="list-style-type: none"> <li>Higher finance costs in both the international and domestic capital market</li> </ul>	Stable
<b>Liquidity</b>	<ul style="list-style-type: none"> <li>Access to excess CRR via special bills</li> </ul>	<ul style="list-style-type: none"> <li>Excess CRR debits</li> </ul>	Stable
<b>Overall</b>			<b>Stable</b>

Valuation and Fundamental Metrics																
	Fundamentals					Trailing				Valuation						
	NIM	CoF	CIR	CAR	NPL	EPS	BVP	P/E	P/BV	Exp Div Yield	Target PE	Exp. EPS	2023 TP	CP	UPP	RT
ACCESSCORP	5%	3%	66%	23%	4%	4.93	29.11	1.72x	0.29x	11.18%	1.63	6.41	10.46	8.50	+23%	BUY
ETI	5%	2%	56%	15%	6%	6.50	30.80	1.63x	0.34x	6.98%	2.22	6.38	14.14	10.60	+33%	BUY
FCMB	7%	4%	69%	15%	5%	1.52	13.31	2.54x	0.29x	5.95%	2.60	1.64	4.26	3.85	+11%	BUY
FIDELITYBK	6%	4%	70%	20%	3%	1.34	11.01	3.24x	0.39x	12.24%	2.51	2.23	5.61	4.35	+29%	BUY
FBNH	5%	2%	67%	16%	6%	5.62	24.89	1.94x	0.44x	3.21%	3.89	3.62	14.08	10.90	+29%	BUY
GTCO	7%	1%	49%	22%	6%	5.97	29.66	3.85x	0.78x	13.04%	3.81	6.69	25.51	23.00	+11%	BUY
STANBIC	4%	2%	60%	20%	3%	5.57	29.34	6.00x	1.14x	10.94%	6.72	5.75	38.67	33.45	+16%	BUY
STERLN BANK	8%	3%	76%	15%	1%	0.61	5.19	2.31x	0.27x	7.07%	2.62	0.58	1.53	1.40	+9%	HOLD
UBA	6%	2%	63%	30%	3%	3.80	24.15	2.00x	0.31x	13.03%	1.91	4.93	9.43	7.60	+24%	BUY
UBN	4%	4%	76%	15%	4%	0.67	9.63	9.56x	0.66x	0.00%	9.13	0.75	6.84	6.40	+7%	HOLD
WEMABANK	3%	5%	82%	12%	4%	0.28	1.88	13.84x	2.08x	8.62%	4.22	0.84	3.55	3.90	-9%	HOLD
ZENITHBANK	7%	1%	58%	21%	4%	8.23	40.52	2.92x	0.59x	12.92%	3.07	8.68	26.69	24.00	+11%	BUY

Kindly note the following legends for the fundamentals tables.

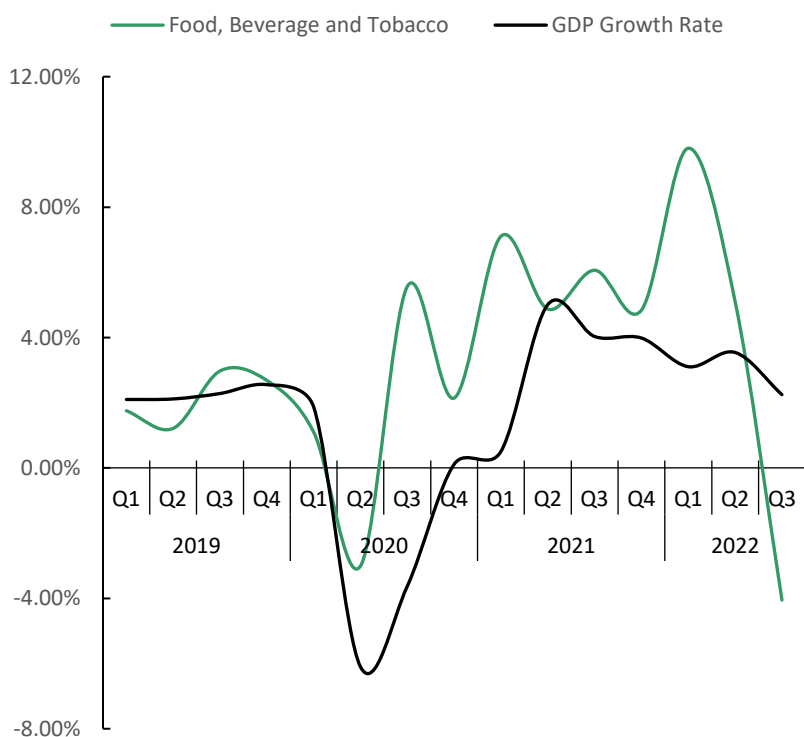
**NIM**= Net Interest Margin; **CoF** = Cost of Funds; **CIR** = Cost to Income Ratio; **CAR** = Capital Adequacy Ratio; **NPL** = Non-Performing Loan Ratio  
**\*TP** calculated with EV/EBITDA multiple. **BVP**= Book Value Per Share  
**TP**=Target Price **P/E**=Price to Earnings Ratio  
**CP**= Price as at December 30, 2022 **AT**=Asset Turnover  
**UPP**=Upside Potential **OM**=Operating Margin  
**RT**= Rating **NM**= Net Margin  
**Exp. EPS**= 2022 Dec Expected EPS **Lev**=Leverage  
**EV/EBITDA**= Enterprise Value to EBITDA Ratio **EBITDA**=Earnings Before Interest, Tax, Depreciation and Amortization  
 Data in the Fundamental columns are based on trailing performance.

# Consumer Goods

## A Year of Severe Turmoil: Going Through an Exigent Phase

Although the expanding demographics and essential nature of most products that constitute the consumer goods basket have remained the major driver of demand in the consumer goods sector; the sector have experienced significant difficulties. Rising commodity prices, currency devaluation, dwindling consumer purchasing power, and security challenges are the major factors impacting the sector's performance. Thus, earnings recorded by most players in the sector have been broadly unimpressive. Our proxy measure of the consumer goods sector output (the food and beverage sector GDP) suggests that the sector's overall performance has been underwhelming as the food and beverage sector recorded a 4.05% YoY contraction in Q3:2022 (vs +6.07% YoY Q3:2021), representing its first contraction since Q1:2021.

**Chart 58: GDP and Food, Beverage Sector Growth (YoY)**



Source: National Bureau of Statistics, Meristem Research

## Resilient Despite Mounting Pressures

Despite the multiple headwinds impacting the consumer goods sector, players have sustained a uniform increase in topline through investment in capacity expansion, price increases, increased product portfolio, volume growth and further backward integration investment. Thus, the average revenue growth for the listed players as of 9M:2022 settled at 34.74% YoY. Some of the most notable revenue growth was recorded by **CADBURY** (+41.58% YoY), **FLOURMILL** (+37.82% YoY), **NASCON** (+62.76% YoY), and **DANGSUGAR** (47.48% YoY). With the continuous implementation of growth initiatives and sustained domestic demand, turnover is expected to maintain an uptrend in the near term.

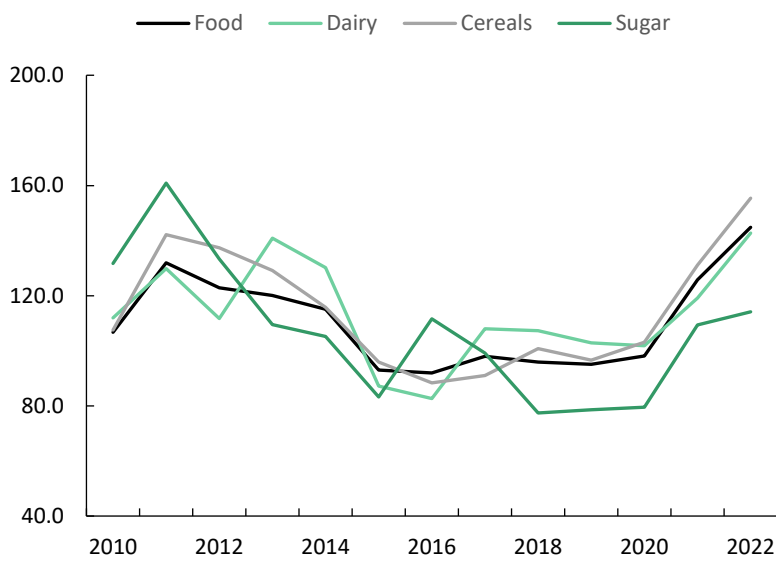
## Bottom-line Pressured by Surging Costs

Based on the most recent earnings releases, the bottom-line performance has been primarily mixed, with players either experiencing slower earnings growth or a significant decline in earnings momentum. Notably, **FLOURMILL**, **UACN**, and **UNILEVER** recorded significant earnings contraction despite the deployment of several growth initiatives during the course of the year.

The dual effects of the rapid increase in global commodity prices and FX illiquidity have been the major factors driving the growing gap between turnover growth and earnings momentum. According to the Food and Agriculture Organisation (FAO) of the United Nations, the global food index expanded by 15.22% YoY in December 2022, with the prices of cereal, sugar and dairy products increasing by 18.74% YoY, 4.45% YoY and 19.85% YoY, respectively.

Although the substantial increase in the global food index further justifies the growing narrative of the global increase in commodity prices, the recent fuel scarcity and higher cost of borrowing (following the continued increase in MPC rate) is expected to worsen production activities, further affecting the 2022FY earnings prospect.

**Chart 59: Movement in FAO Selected Food Index**



Source: FAO, Meristem Research

*On a balance of factors, we maintain a moderate posture for the consumer goods companies in 2023, driven by sustained domestic demand, implementation of expansion initiatives and growing demographics. However, with no end in sight to the Russian-Ukraine crisis, commodity prices are expected to maintain an upward trend mounting further pressure on production costs. Furthermore, with the lingering economic uncertainties (fuel scarcity, rising inflation, foreign exchange scarcity) we expect production costs to remain elevated which would adversely impact earnings potential.*

## Flour millers: Wheat Imports to Remain Significant

Global wheat production was largely pressured in 2022. The United State Department of Agriculture (USDA) estimates that production will settle at 779.33MMT in 2022 (a paltry 0.64% increase compared to 774.55 million metric tonnes (MMT) in 2021) as the geopolitical tensions, drought conditions, and heat wave in wheat-producing areas have negatively impacted the wheat value chain. These accompanied with other supply chain disruptions (increased shipping costs, labour shortages and energy price shocks) have led prices significantly higher. As of November 2022, both the Food and Agricultural Organization (FAO) and World Bank reported an 11.90% YoY increase in price of the commodity.

Given Nigeria’s exposure to wheat imports, these conditions impacting the global scene have made the operating environment mostly challenging for flour millers in the country. According to the National Bureau of Statistics, as of 9M:2022, wheat remained amongst the top three imported items (NGN753.60bn) in Nigeria. Thus, cost pressures arising from high inflationary pressure, volatile exchange rate environment, supply chain disruption and high raw material prices on the global scene set the tone for uptick in prices across major wheat-based products and its complements.

To limit the impact of these global challenges on domestic availability of the commodity, industry players in Nigeria are intensifying their backward integration efforts to manage any potential surprise. As of September 2022, Crown Flour Mills NGN300mn 10-year project which was launched in 2021, achieved its first milestone of producing 10 kilograms of the seed varieties. The 10 kilograms of pre-multiplication wheat seeds are expected to be cultivated on 1 million square foot plots during the next planting season.