

Cowry Asset Management Limited

(member of The Nigerian Stock Exchange)



H1 2020 Review; Expectations and Investment Strategies in H2 2020

By

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Life is under no obligation to give us what we expect – Margaret Mitchel

COMING INTO 2020....

- Nigeria's real Gross Domestic Product grew year-on-year (y-o-y) by 2.27% to N71.39 trillion in 2019, faster than 1.19% growth to N69.80 trillion registered in 2018.
- The non-oil sector which accounted for the improved GDP number grew y-o-y by 2.06% to N65.12 trillion.
- Also, Oil & Gas sector expanded y-o-y by 4.59% to N6.27 trillion in 2019, chiefly due to a 4.69% increase in crude oil output to 2.01 million barrels per day in 2019. This was in spite of a 10.02% decline in crude oil (Bonny Light) prices to USD65.12 a barrel.



- Meanwhile, Nigeria's external reserves fell y-o-y by 10.57% to USD38.09 billion.
- Naira/USD exchange rates closed mixed at the end of 2019. Naira appreciated at the BDC and parallel market segments by 0.28% each to close at N358/USD and N362/USD respectively. However, it depreciated at interbank and I&E FX window by 0.06% and 0.14% to N358.51/USD and N364.51/USD respectively.
- Inflation rate climbed from 11.4% in January 2019 to December 2019 was 12.0% (11.4% as at December 2018).



- Monetary Policy rate remained flat at 13.50% in 2019 while interest rates were generally lower on average in 2019 compared to 2018.
- Specifically, savings deposit rate fell to 3.84% in 2019 (from 4.07% in 2018), 3 months deposit rate plunged to 8.90% in 2019 (from 9.70% in 2018). Prime lending rate and maximum lending rate also fell to 15.61% and 30.76% in 2019 (from 16.91% and 31.10% in 2018).



- Nigerian Treasury Bills Rates also declined amid increased demand (flight to safety) and excess liquidity. 91-day bills, 182-day bills and 364-day bills fell to 9.77%, 11.33% and 12.21% in 2019 (from 10.96%, 12.11% and 12.77% in 2018).
- Nigerian equities market underperformed in 2019 with the All Share Index falling by 14.60% to 26,842.07 points. However, market capitalization increased by 10.65% to N12.97 trillion, mainly on account of new listings of MTN and Airtel shares.



Nigeria's Major Macroeconomic Indicators

Nigeria's GDP	2018	2019
Amount (N 'Bn)	69,799.94	71,387.83
<i>Y-o-Y Growth Rate</i>	1.91%	2.27%
Oil Sector (N 'Bn)	5,995.88	6,270.86
<i>Y-o-Y Oil Growth Rate</i>	0.97%	4.59%
Non-Oil (N 'Bn)	63,804.07	65,116.97
<i>Y-o-Y Non-Oil Growth Rate</i>	2.00%	2.06%

Average Oil Statistics	2018	2019
Oil Production (Mbpd)	1.92	2.01
<i>y-o-y Growth Rate</i>	1.59%	4.69%
Bonny Light (USD/bbl)	72.37	65.12
<i>y-o-y Growth Rate</i>	32.33%	-10.02%

Nigeria's FX Reserves	2018	2019
Amount (N 'USD)	42,594.84	38,092.72
<i>y-o-y Growth Rate</i>	8.24%	-10.57%

	Interbank	I&E FX Window	BDC	Parallel Market
2019 Close	358.51	364.51	358	362
2018 Close	358.31	364	359	363
<i>Percentage Change</i>	0.06%	0.14%	-0.28%	-0.28%

Source: National Bureau of Statistics, Central Bank of Nigeria, Cowry Research

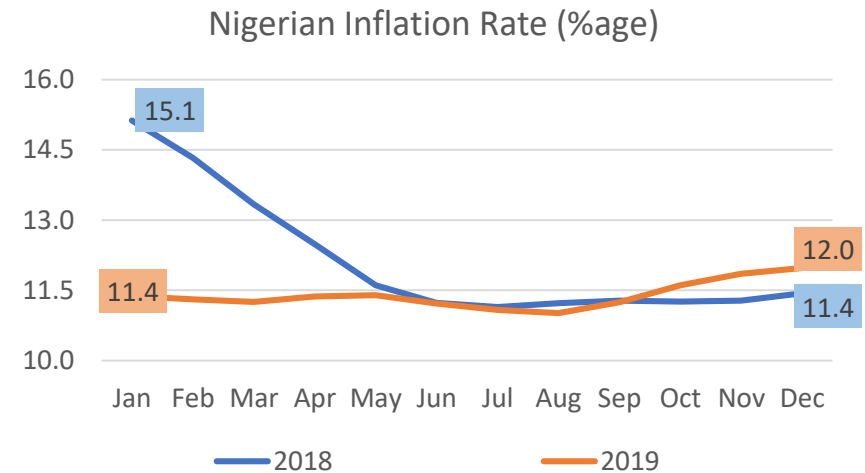
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Nigeria's Major Macroeconomic Indicators

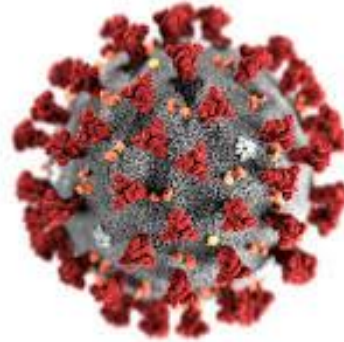
	91-day Bills	182-day Bills	364-day Bills
2019 Average Rates	9.77	11.33	12.21
2018 Average Rates	10.96	12.11	12.77

Average Interest Rates	2019	2018
Savings Deposit	3.84%	4.07%
1 Month Deposit Rate	8.30%	8.92%
3 Months Deposit Rate	8.90%	9.70%
6 Months Deposit Rate	10.07%	10.48%
12 Months Deposit Rate	10.15%	10.31%
Prime Lending Rate	15.61%	16.91%
Max Lending Rate	30.76%	31.10%

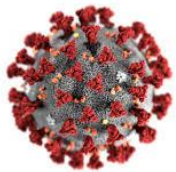


Equities Performance	2019	2018	%age Change
NSE ASI	26,842.07	31,430.50	-14.60%
Market Capitalization	12,968.59	11,720.72	10.65%

Market Capitalization rose mainly on account of the listing of MTN and Airtel



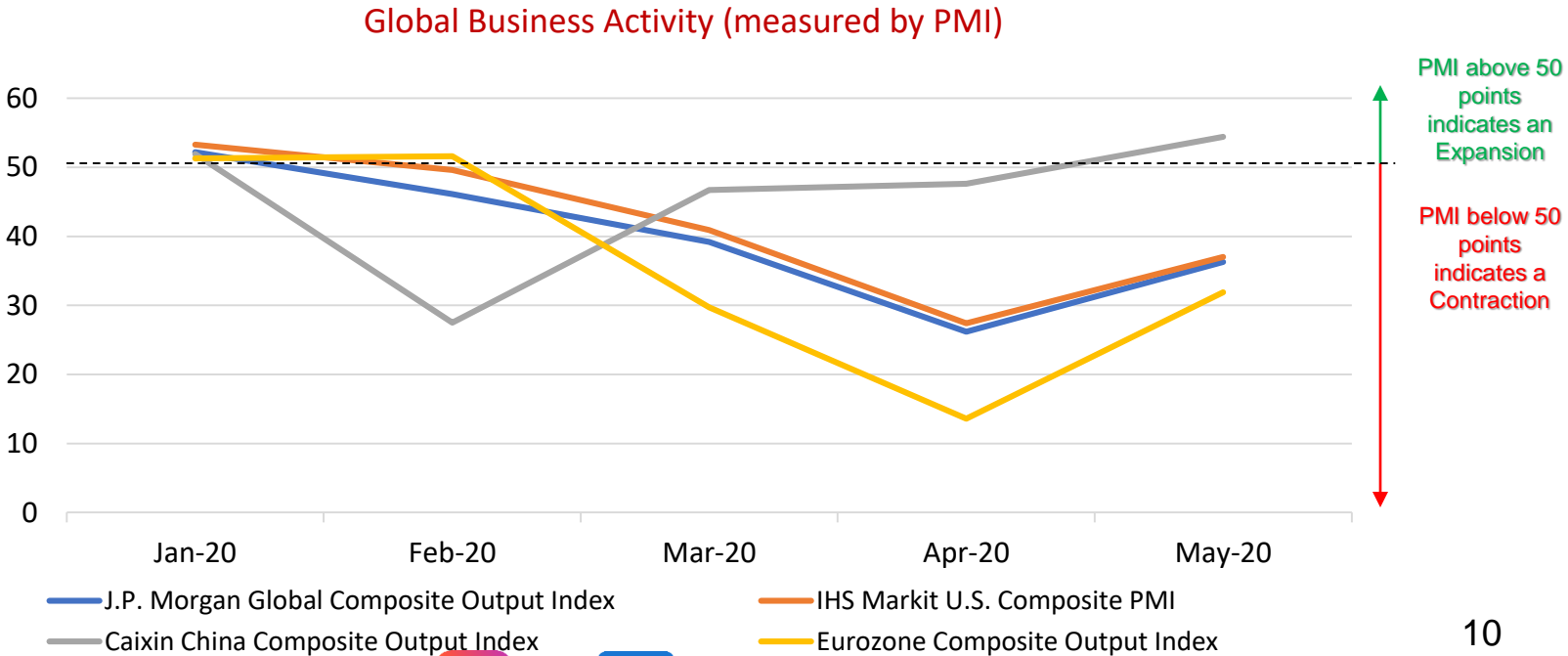
H1 2020 IN THE NUTSHELL



- H1 2020 was overshadowed by the widespread COVID-19 pandemic which precipitated border closures, export restrictions of critical medical supplies, business shutdowns, demand and supply shocks and initial panic across the financial markets. These basically shaped the theme for the global economy, which fell into recession in H1 2020.



- Global economic powers such as the United States, China (from where the pandemic began and was exported to the rest of the world) and Eurozone (which bore the brunt of the catastrophe), all witness contractions in March, April and May in both manufacturing and non-manufacturing business activities. Notably, the Chinese economy was amongst the first to exit the global recession.

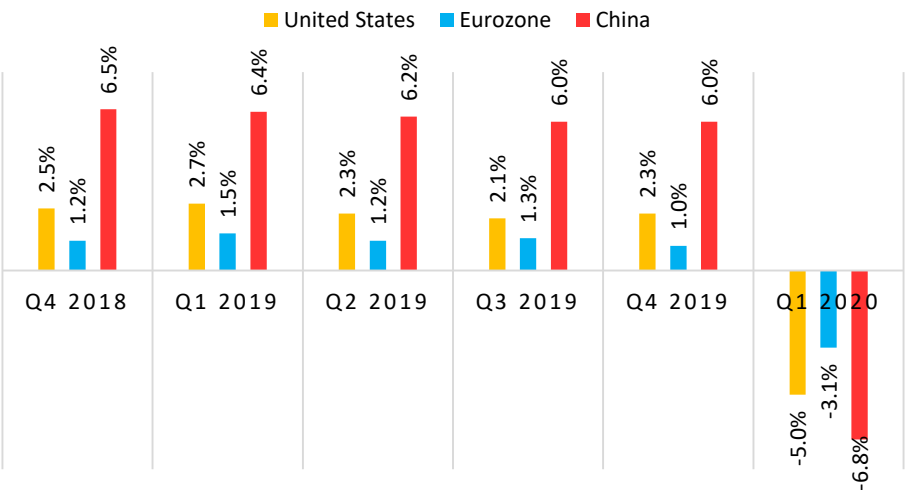


Source: Markit Economics, Cowry Research

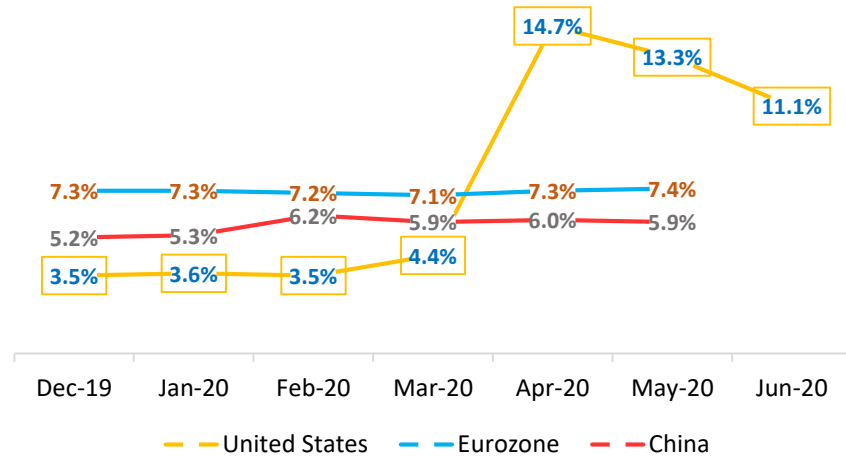


- In Q1 2020, China and Eurozone recorded declines in GDP Growth rates of -6.8% and -3.1% respectively while the United States recorded GDP contraction of -5%. Unemployment rates also increased across the globe as a result of the lockdowns and decline in global demand.

Y-O-Y GDP GROWTH RATE OF MAJOR ECONOMIES



UNEMPLOYMENT RATES OF MAJOR ECONOMIES



- On account of an abrupt slowdown in global demand, especially for commodities such as crude oil, there ensued a hot race by oil rich economies to sell their fast depreciating cargoes to unenthusiastic refineries which were negatively affected by weakened demand for their refined products. This was exacerbated by a volume war between Saudi Arabia and Russia which invariably led to a glut in crude oil and an overwhelmed storage capacity both onshore and offshore.
- In response, global investments in the oil and gas space plunged while oil producers moved to cut production. Specifically, OPEC+ agreed to cut production by 9.7 million barrels per day (mbpd) in May. Similarly, other global players cut around 3.6 mbpd as at May 2020.

	2020f	Jun-20e	2019e	%Change
World Oil Demand mb/d	90.72	-	99.67	-8.98%
World Oil Supply mb/d	90.00*	86.29	99.17	-9.24%
Non Opec Supply mb/d (plus NGLs)	61.76	64.02	65.03	-5.03%
Opec Supply mb/d (plus NGLs)	28.24*	22.27	34.14	-17.26%
World Economic Growth Rate	-3.4%	-	2.9%	-

Source: Opec, Cowry Research; *Cowry Research Estimates

Crude Oil Marker		Year high	Year low	Peak Rebound	
West Texas Intermediate		31-Dec-19	2-Jan-20	21-Apr-20	30-Jun-20
		\$61.68/b	\$61.18/b	\$11.57/b	\$39.27/b
	<i>Change from 2019 year end</i>		-0.8%	-81.2%	-36.3%
Brent		31-Dec-19	9-Jan-20	21-Apr-20	30-Jun-20
		\$66.67/b	\$68.91/b	\$19.33/b	\$42.27/b
	<i>Change from 2019 year end</i>		3.4%	-71.0%	-36.6%
OPEC Reference Basket		31-Dec-19	9-Jan-20	22-Apr-20	30-Jun-20
		\$67.96/b	\$70.89/b	\$12.22/b	\$38.22/b
	<i>Change from 2019 year end</i>		4.3%	-82.0%	-43.8%

Source: OilPrice.com, Cowry Research





- On their part, both fiscal and monetary policies put in place stimulus packages to alleviate the pain of households and businesses and to spur rebound in economic activities while also issuing COVID-19-related guidelines to curtail the spread of the pandemic as they eased the lockdown.
- These measures helped to facilitate economic recovery, albeit gradually, and raised optimism of a “V-Shaped” recovery as resonated by the improved performance of major stock exchanges, especially in the United States.

Country	Fiscal Stimulus Package	Monetary Stimulus Package and Policy Moves	
The United States	\$2.8 trillion	\$3.97 trillion	Fed funds rate reduced to 0.00%-0.25% (from 1.50%-1.75%). Discount rate, also cut by 1.5% to 0.25%.
China	\$0.873 trillion	\$0.983 trillion	PBOC cut the one-year Prime rate down to 3.85% (from 4.15%) and the five-year Prime rate down to 4.65% (from 4.80%). Cut its seven-day repo rate to 2.20% (from 2.40%).
European Union	\$0.860 trillion	\$1.608 trillion	ECB left deposit interest rate negative and refinancing interest rate at zero.
Germany	\$0.964 trillion	-	Ditto
United Kingdom	\$0.6 trillion	0.76 trillion	BOE cut its benchmark rate twice, to 0.25% (from 0.75%), and then to 0.1% (from 0.25%).
Japan	\$2.108 trillion	\$1 trillion	BOJ's lending program expanded to provide 1-year zero-interest loans to financial institutions to lend to affected SMEs
India	\$0.035 trillion	\$0.062 trillion	RBI cut its benchmark repo rate by 0.75% to 4.4 and again by 0.25% to 3.75%. Reverse repo rate also cut by 0.9% to 4%.
Nigeria	-	\$9.18 billion	CBN cut MPR by 1% to 12.50%

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Global Stock Markets Performance		Year high	Year low	
	31-Dec-19	11-Feb-20	23-Mar-20	30-Jun-20
Dow Jones Industrial Average	28,538.44	29,551.42	18,591.93	25,812.88
<i>Change from 2019 year end</i>		3.5%	-34.9%	-9.6%
	31-Dec-19	11-Feb-20	23-Mar-20	30-Jun-20
NASDAQ Composite Index	8,972.60	10,020.35	6,860.67	10,058.77
<i>Change from 2019 year end</i>		11.7%	-23.5%	12.1%
	31-Dec-19	17-Feb-20	18-Mar-20	30-Jun-20
German Stock Index DAX	13,249.01	13,789.00	8,441.71	12,310.93
<i>Change from 2019 year end</i>		4.1%	-36.3%	-7.1%
	31-Dec-19	5-Mar-20	23-Mar-20	30-Jun-20
Shanghai Shenzhen CSI 300 Index	4,096.58	4,206.73	3,530.31	4,163.96
<i>Change from 2019 year end</i>		2.7%	-13.8%	1.6%
	31-Dec-19	20-Jan-20	19-Mar-20	30-Jun-20
Nikkei 225	23,656.62	24,083.51	16,552.83	22,288.14
<i>Change from 2019 year end</i>		1.8%	-30.0%	-5.8%

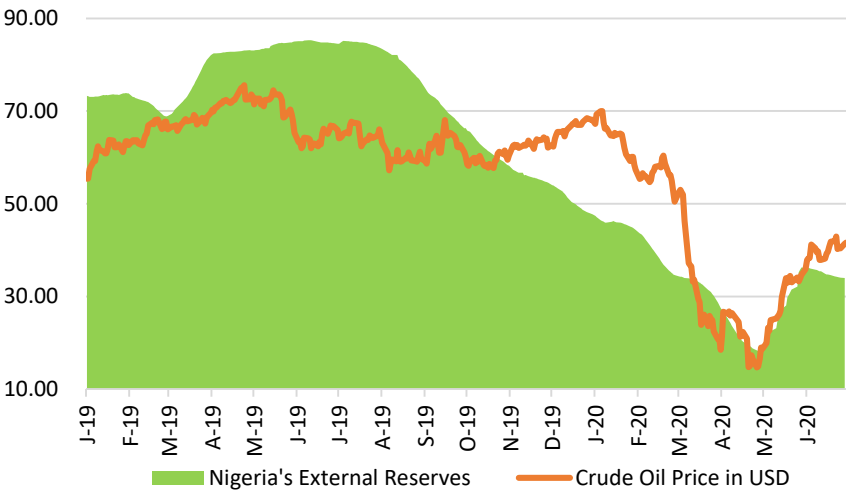


NIGERIAN ECONOMY

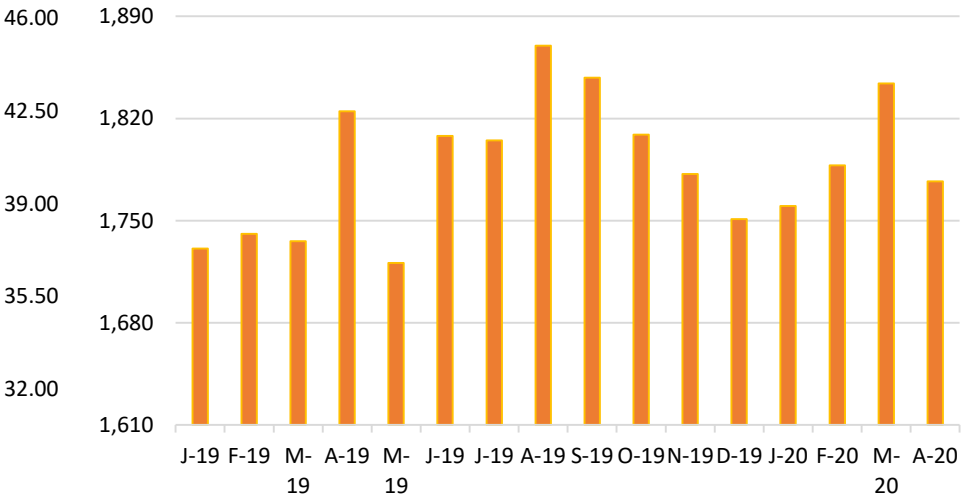


- Nigeria’s economy was hit by external shocks as the price of Bonny Light grade plunged to USD14.67 a barrel as at April 27, 2020 (from USD68.10 a barrel as at December 31, 2019) while the external reserves plummeted to USD33.43 billion as at April 29, 2020 (from USD38.60 billion as at December 31, 2019) amid lower prices and production output.

Nigeria's External Reserves and Crude Oil Price

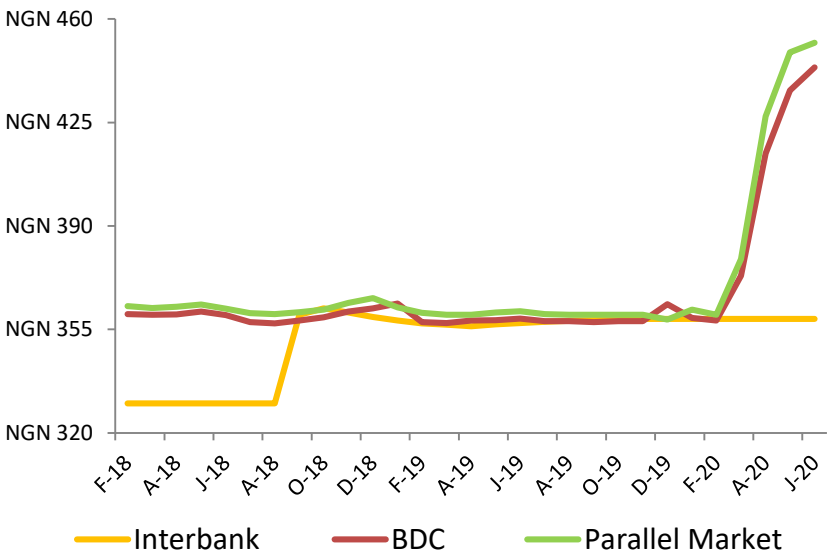


Nigeria's Daily Crude Oil Output

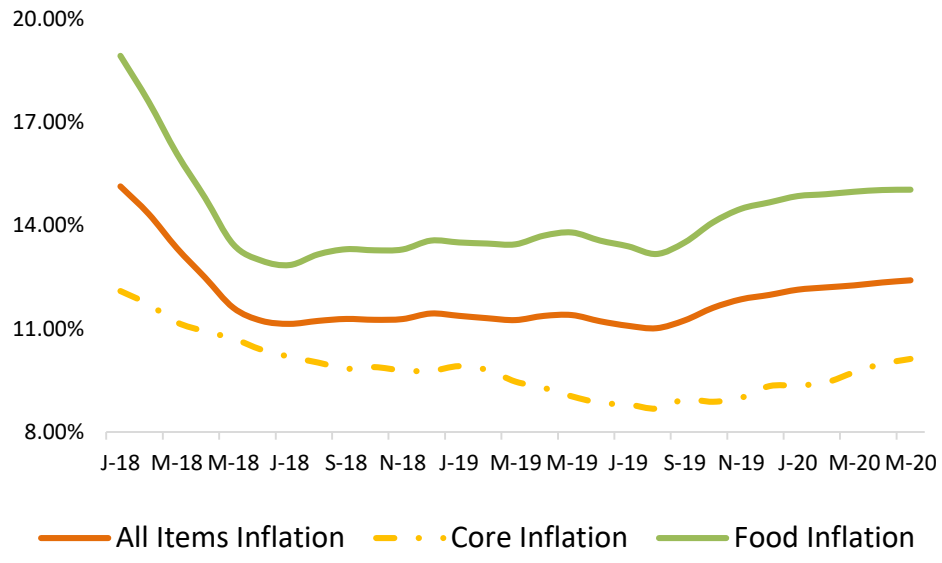


- Following plunge in external reserves, the NGN/USD exchange rate spiked. Meanwhile, inflation rate continued to climb, albeit gradually.

Monthly Average Exchange Rates (NGN/USD)

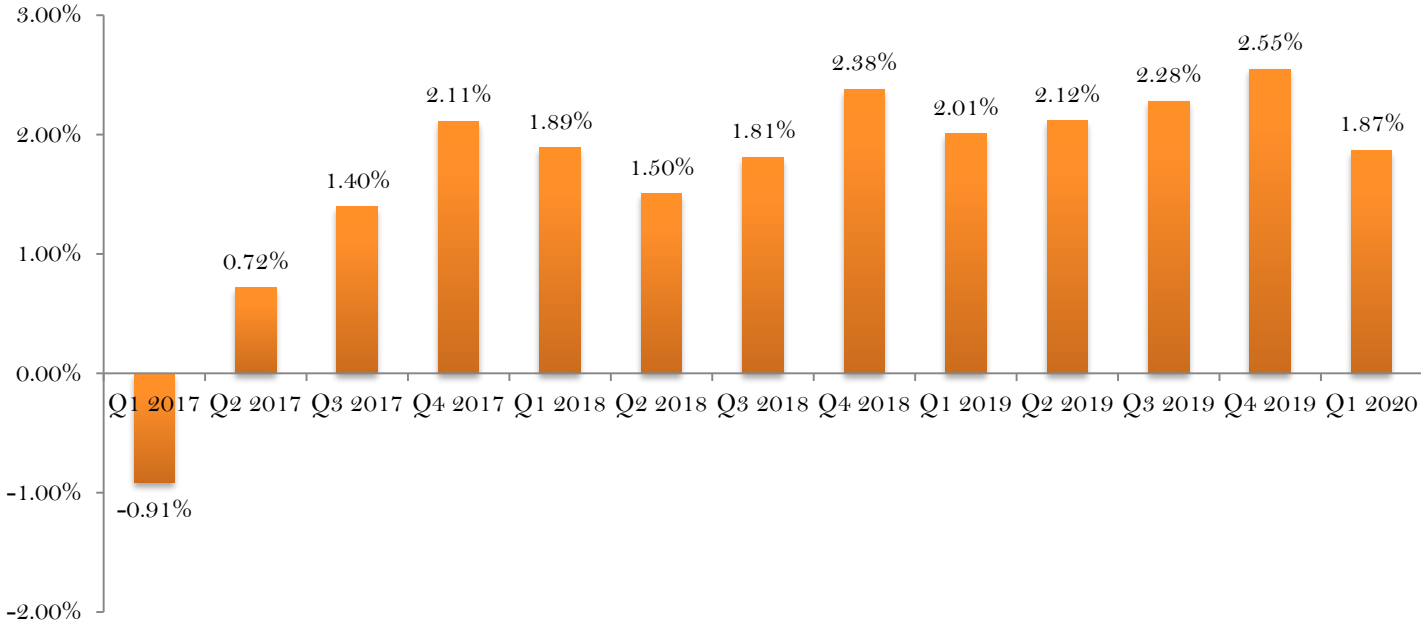


Consumer Price Inflation



- In Q1 2020, Nigeria’s GDP grew BY 1.87%, slower than 2.55% in Q4 2019 (and 2.01% in Q1 2019). Growth was driven by positive, albeit slower, growth in oil & gas and non-oil sectors by 5.06% and 1.55% from 6.36% and 2.26% respectively.

Y-o-Y Real GDP Growth Rates



Major Sectors	Q1 2020	Q4 2019	Q-o-Q %Change
Oil & Gas (N 'Trn)	1.591	1.429	11.30%
Y-o-Y %Change	5.06%	6.36%	
Non-Oil Sector (N 'Trn)	15.151	18.098	-16.29%
Y-o-Y %Change	1.55%	2.26%	
Quarter GDP (N 'Trn)	16.742	19.527	-14.27%

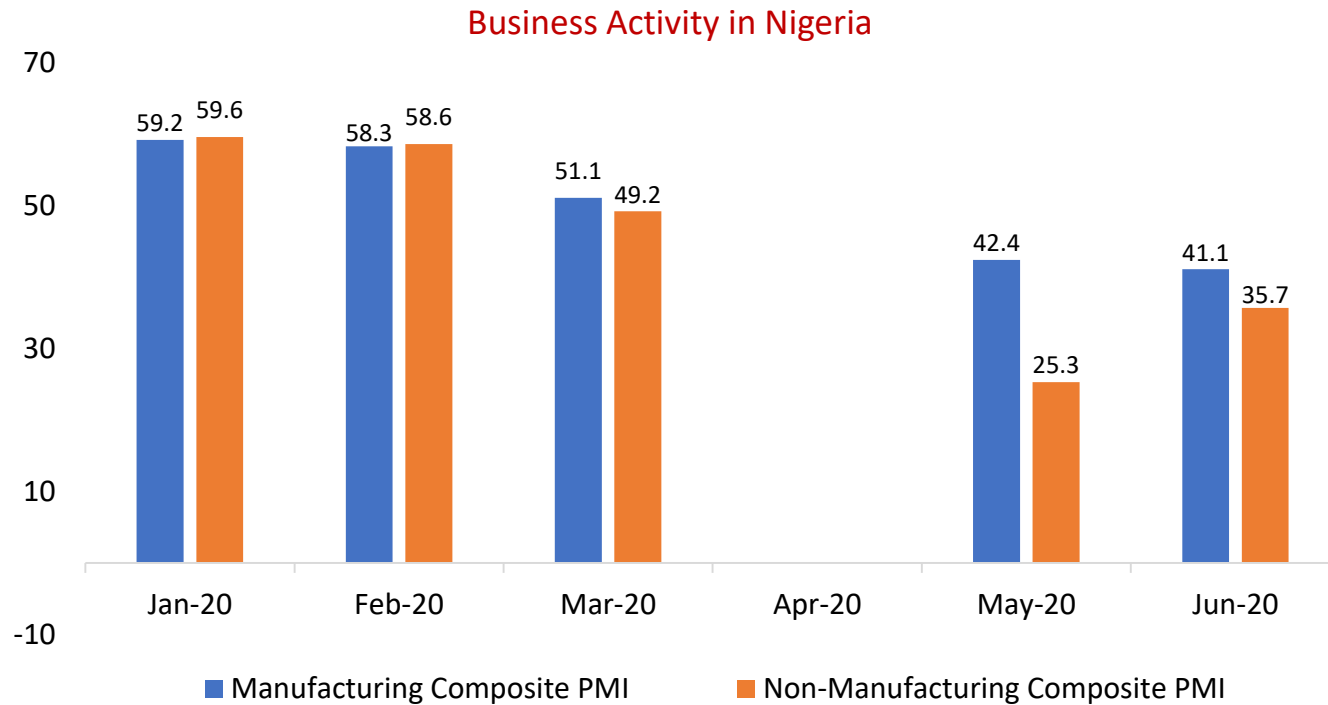
Share of Real GDP (%)	Q1 '20 Share of Real GDP	Q1 '20 y-o-y Growth (%)	Q4 '19 y-o-y Growth (%)
Agriculture	21.96%	2.20%	2.31%
Trade	16.08%	-2.82%	-0.58%
Info & Comm	14.07%	7.65%	8.50%
Manufacturing	9.65%	0.43%	1.24%
Mining & Quarrying	9.54%	4.58%	6.07%
Real Estate	5.21%	-4.75%	-3.45%
Construction	4.08%	1.69%	1.31%
Financial Services	3.81%	20.79%	20.18%
Profes, Sci & Tech Services	3.42%	-0.39%	0.55%
Education	2.08%	0.69%	0.84%
Other Economic Activities	10.10%		
7/29/20 Qtr 2019 Real GDP	N16.74 Trn	1.87%	2.55%



Impact of COVID-19 on Businesses

- Businesses activities in manufacturing and non-manufacturing sectors, entered into contraction territory in Q2 2020 in the thick of the pandemic.
- The contraction in manufacturing composite PMI was due to decline in new orders index to 36.4 in June 2020 (from 59.7 in January 2020), which resulted in lower production – the production index decreased further to 36.6 (from 59.6).
- Number of new hires recorded by manufacturers declined in tandem with the lower production volume – the index for employment fell to 35.7 points in June 2020 (compared to 56.9 points in January 2020).

- Meanwhile, the non-manufacturing sector also recorded contraction as its composite PMI fell to 35.7 index points in June 2020 (from 59.6 index points in December 2019).
- This was driven by contraction in business activity to 34.3 (from 59.8). The non-manufacturing sector also saw contraction in incoming business as well as employment.



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Impact of COVID-19 on Households

- According to a survey in May by National Bureau of Statistics, the impact on employment and income have also been widespread:
- 42% of respondents who were working before the outbreak reported that they were not currently working due to COVID-19.
- 79% of respondents reported that their household total income have decreased since mid-March.
- The most widely reported shock experienced by households was an increase in prices of major food items faced by 85% of households surveyed with 51% of all households resorting to reducing food consumption.

Central Bank of Nigeria Policy Response

- In order to soften the blows of the pandemic to the economy, CBN announced a policy response timeline during which it would provide a combined stimulus package of about N3.5 trillion in targeted measures to households, businesses, manufacturers and healthcare providers; a move also aimed at building a more resilient, more self-reliant Nigerian economy.

Under its Immediate-Term Response, CBN activated the following:

- Ensure financial system stability by granting regulatory forbearance to banks to restructure terms of facilities in affected sectors;
- Grant additional moratorium of 1 year on CBN intervention facilities;
- Reduce interest rates on intervention facilities from 9 percent to 5 percent;
- Create N50 billion targeted credit facility for affected households and SMEs;
- Improve FX supply to the CBN by directing all oil companies (international and domestic) and all related companies (oil service) to sell FX to CBN and no longer to the NNPC;
- Provide additional N100b intervention in healthcare loans to pharmaceutical companies, healthcare practitioners intending to expand/build capacity;
- Provide N1 trillion in loans to boost local manufacturing and production across critical sectors

The Equity Market

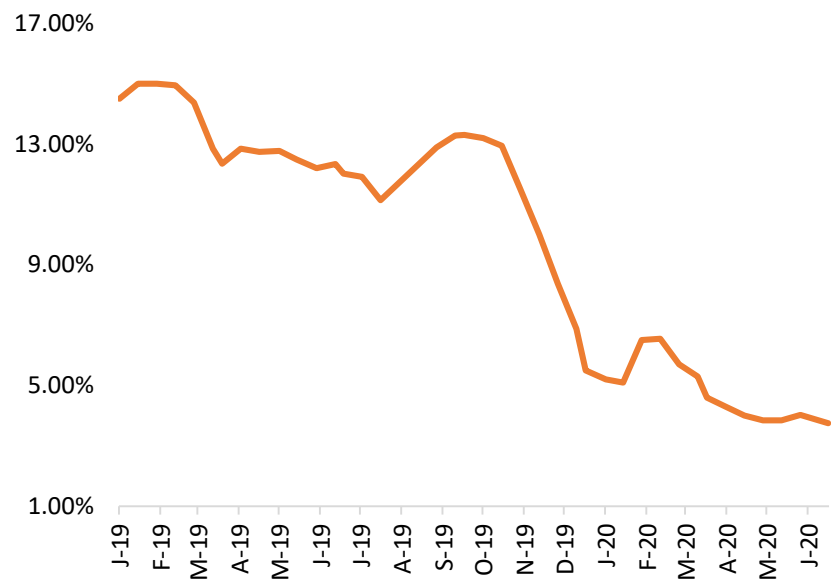
- After posting a loss of 14.6% in 2019, the Nigerian equity market jumped to an excellent start in the first few weeks of the year, posting a world best YTD return of 10.70% on January 20, 2020. However, any hope of a reversal of the two-year consecutive losses posted by the NSE all share index was short-lived as the Covid-19 pandemic took hold, grinding global economies to a halt and sending oil prices tumbling with the Brent crude price touching \$19.3/b in April 2020.
- The NSE ASI went from 26,842.07 at the beginning of January 2020 to 20,669.38 in April (shedding over 20%), before recovering slightly to 24,479.16 at the end of June 2019.

The Bond Market

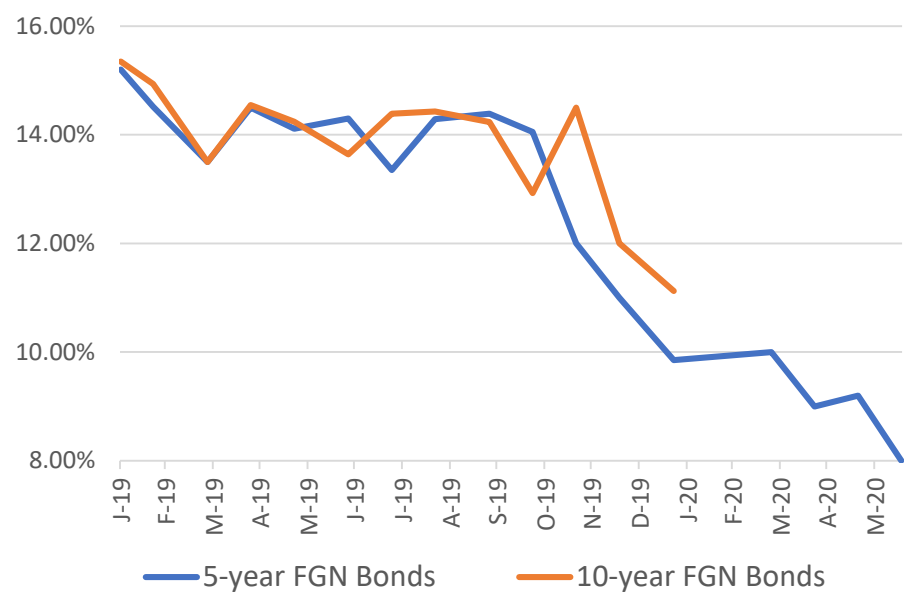
- Interest rates generally moved southwards in the first half of 2020 amid liquidity glut created by a Central Bank of Nigeria directive which banned high net worth individuals and non-bank financial institutions from participating in its Open Market Operations with effect from October 23, 2019.
- Against the backdrop of sustained monetary policy easing, high system liquidity, we saw increased demand for short- and long-term Federal Government debt instruments which resulted in sustained crash in domestic spot rates – 364-day T-Bills fell to 3.75% in June 2020 (from 5.50% in December 2019) while 5-year FGN Bonds fell to 8% in June 2020 (from 11% in December 2019).



Stop Rates of 364-day T-Bills



Stop Rates of Auctioned FGN Bonds



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OUTLOOK

“I like the night. Without the dark, we’d never see the stars” – Stephenie Meyer

GLOBAL OUTLOOK

A few questions beckons

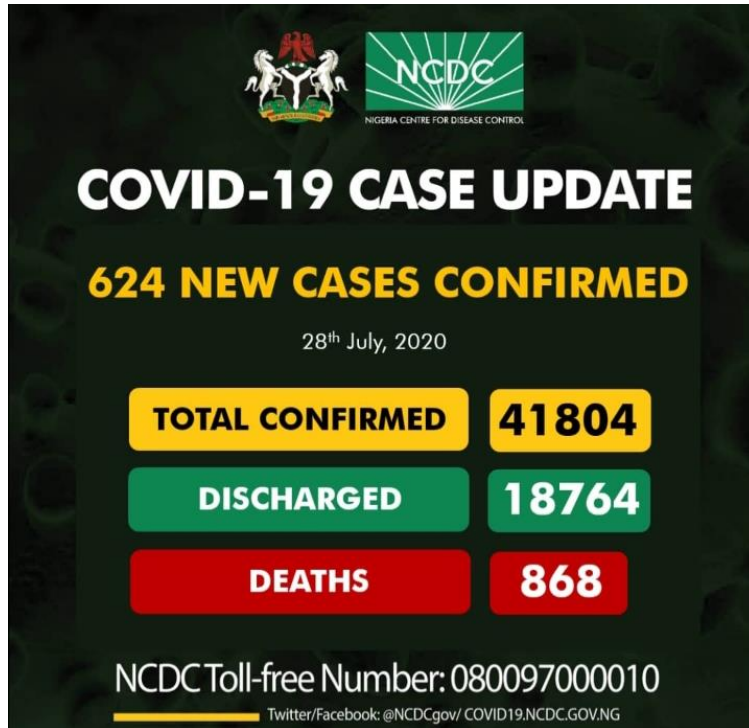
- Is there another wave of the pandemic brewing in the world major markets (United States, China and the Eurozone)
- What more harm can this health crisis do to the health and economic system of the Sub Saharan Africa.
 - Are we facing a 'V shaped' or 'U shaped' recovery?

IMF's Regional Output Forecasts	2019est	2020f
World Output	2.9	-4.9
Advanced Economies	1.7	-8
United States	2.3	-8
Eurozone	1.2	-10.2
Emerging Market and Developing Economies	3.7	-3
China	6.1	1
Sub-Saharan Africa	3.1	-3.2
Nigeria	2.2	-5.4



- Global economy to witness negative growth – IMF predicts decline in global output by 4.9%. We however project gradually recovery from recession amid early expansionary programs and policies by fiscal and monetary authorities which should stimulate consumer demand, spending and hiring by businesses and resumption of global trade.
- Recovery in crude oil prices to range between USD40 to USD50 per barrel amid supply cut and increasing demand, as the United States, China and the Eurozone, resume economic activities.
- U.S. Fed Rate to be retained at the current band of 0.00% and 0.25% given the need to sustain economic recovery in the U.S, which might be a bit challenging amid coronavirus pandemic with concerns about the possibility of another wave.

HAS THE COVID-19 CURVE FLATTENED?



As we continue to learn

Is the Nigerian economy facing a ‘V shaped’ or ‘U shaped’ recovery?



Expected Policy Response

Fiscal and Monetary policy

- Low interest rates is expected to stimulate credit expansion to the private sector. This may however be constrained by limited number of quality credit demands occasioned by weak economic recovery.
- Consumer demand will remain weak in H2 2020 due to increased level of unemployment, reduced salaries and limited fiscal capacity of the Federal, states and local governments.
- Inflation rate to trend further north driven by depreciating local currency, increasing cost-reflective Fuel (PMS) prices, electricity tariff, transport and food costs.

Exchange Rate Conundrum

- We have seen the official exchange rate devalued from 307 NGN/USD to 360 NGN/USD in March and 380 NGN/USD in July at the Secondary Market Intervention Sales (SMIS),
- We do not expect much inflows from FPIs, until global economic activities improve further and the uncertainty around FX rate is cleared – CBN is expected to eventually unify exchange rates from all FX windows.
- The parallel market is trading at a premium of almost N100/\$ to the official market as a result of limited supply from CBN.
- For external reserves, we note that ongoing concessionary foreign borrowings should partly cushion the eroding foreign reserves.
- The current account deficit in Q1, 2020 was \$4.88 billion and may persist until 2022 in the short-term.
- In effect, we expect further devaluation of the local currency and possible exchange rate unification.

GENERAL GUIDANCE FOR INVESTING THROUGH THE PANDEMIC

Amid the current market uncertainty, a few general investment lessons will help investors avoid pitfalls in the short-term:

- Incorporate a long-term view into your portfolio decisions
- Diversification will always be key
- Some level of liquidity will always be valuable
- Focus on value
- Your diversification maybe insufficient without Eurobonds
- Cryptocurrencies, agricultural funds and forex trading should be seen as high risk investments.

FIXED INCOME

Expectations

- CBN to retain OMO yield at a relatively high rate in order to attract foreign portfolio investors. So far, CBN has maintained relatively high OMO yield environment (341DAY OMO bills traded at 9.81% as at June 18, 2020)
- An upward shift in the yield curve may be seen in Q4

Our Investment Guidance

- We favor investing in the short-term bonds and in fixed deposits to retain the ability to benefit from the expected upward shift in the yield curve.
- We may see new corporate bond issues as firms look to take advantage to the low yield environment. Focus on Investment grade Instruments with adequate risk premium.

EUROBOND

Expectations

- We expect increased demand for Eurobond as investors struggle to hedge against Naira devaluation.
- We recommend rebalancing of portfolios to include or increase Eurobond instruments.
- We however expect that the current parallel market exchange rate (over 470 \$/NGN) and the size of the minimum deal ticket may limit the number of investors that can take advantage of this class of investment. Retail investors can however access the market through mutual funds and other derivatives.
- Investment grade corporate Eurobond should provide additional rewards to investors.

EQUITY

Expectations

- Anyway you slice it, the Nigerian economy may only recover slowly in the aftermath of the pandemic.
- We expect weak Q2 and Q3 results will drive equities prices lower
- In spite of the OPEC+ agreement and cuts, oils price may not return to the nation's comfort zone (\$60 per barrel) anytime soon.

Our Investment Guidance

- Investors with long term horizon may be facing the best time to take position.
- We advise focus on fundamentally strong companies with low P/E, high dividend yield and historically high Return on Equity (ROE).
- *Sectors less impacted by the pandemic –ICT, healthcare, financial services and agriculture may offer additional value.*

IN CONCLUSION

- While we agree that the Nigerian economy will contract in 2020, we however believe that the contraction will not be as steep as the 5.4% projected by IMF.
- We expect the Agriculture sector which accounts for about 22% of the GDP to remain resilient due principally to favourable weather conditions this year, This is in spite of setbacks from highlighted insecurity in the Northern parts of the country.
- The ICT sector accounts for 14% of the GDP and is expected to maintain its growth momentum in the remaining quarters of the year.
- The Oil & Gas, Trade and Manufacturing sectors are however expected to contract in H2 2020.
- In summary, robust grow in Agriculture and ICT, which combined account for 36% of the GDP will have the effect of cushioning the rate of economic contraction in 2020. We therefore project an economic contraction of 2% - 3%.

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THANK YOU

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(member of The Nigerian Stock Exchange)

