Access Economic Quarterly

Second Quarter 2012

access

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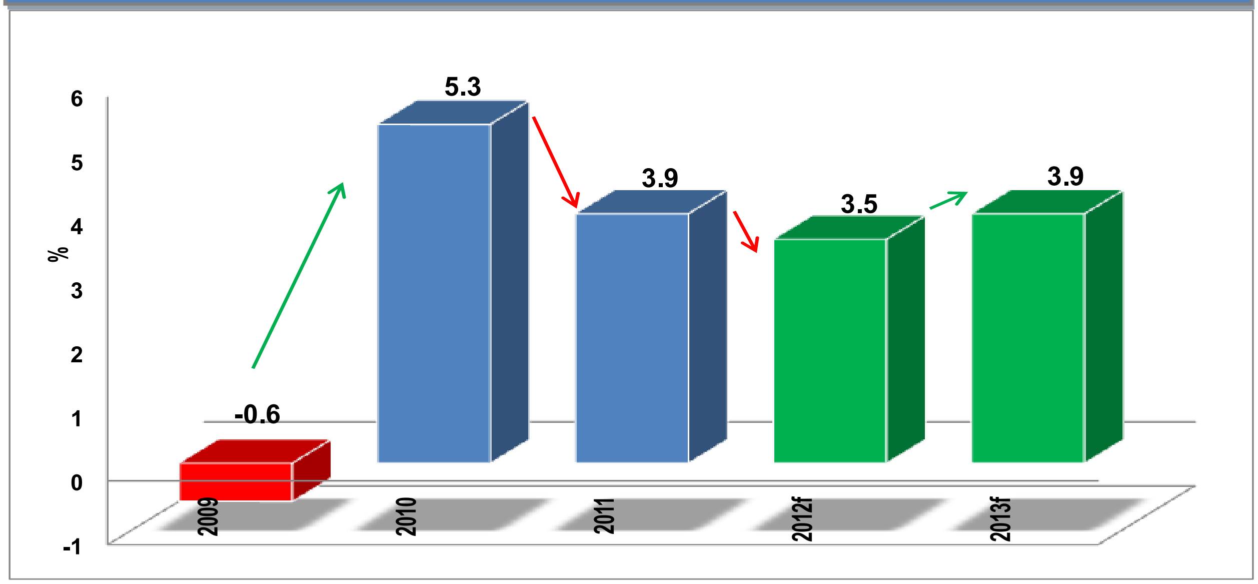
1.0 Global Economy

The global economy showed signs of further weakening in Q2 as financial markets and sovereign stress in the Euro-zone ratcheted up. Growth in a number of major emerging markets also slowed. In advanced economies, unemployment remained high. Global output expansion in Q2 was 3.4% from 3.6% attained in the first three months of the year. The Q1 growth momentum – partly due to easing financial conditions and recovering confidence in response to ECB longer-term refinancing operations (LTROs) – was not sustained in Q2. Risks to financial stability also increased in Q2 2012 following continued slow global economic recovery and fears about the quality of bank assets in Europe.

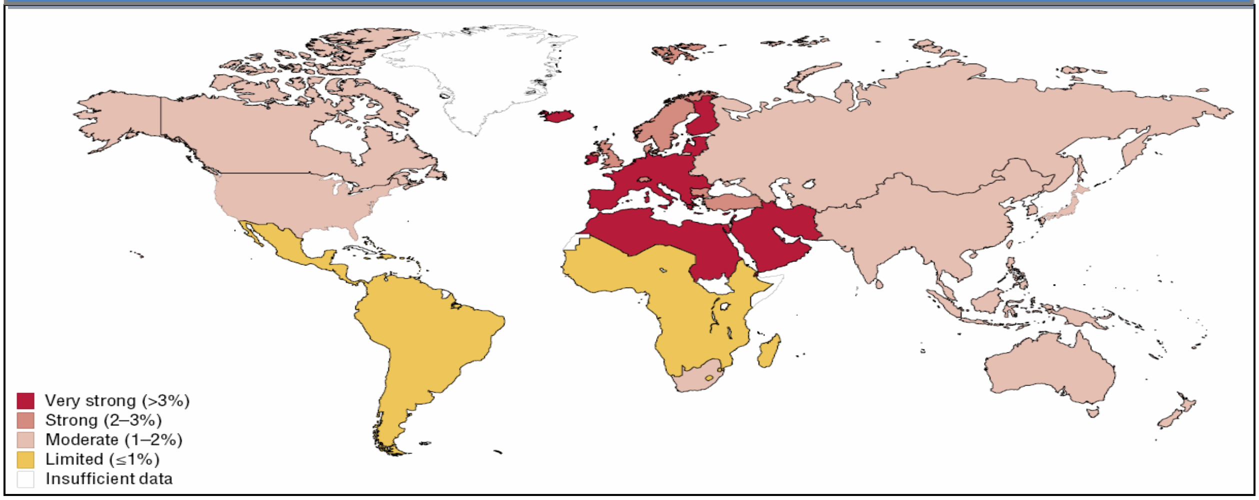
Global GDP Growth



Source: Bloomberg

The fringe economies in the euro area were at the epicenter of further escalation in global financial market stress. This was triggered by increased political and financial uncertainty in Greece and banking sector problems in Spain. The extent of partner-country willingness to help vulnerable economies also dampened enthusiasm. This resulted in escalating pressure manifesting as huge capital outflows and renewed surge in sovereign yields. Other manifestations were further bank deleveraging and contraction in credit to the private sector.

Eurozone Debt Crisis: Impact on Various Regions



Source: IMF

The world economy is projected to grow by 3.5% in 2012.

1.1 United States

The United States economy grew by 1.5% in Q2 2012, down from the 2% posted in Q1 2012. The growth estimate, lower than the 2.5% earlier projected, is blamed on the slump in private consumption expenditure, acceleration in imports and drop in business spending. The world's largest economy continues to expand at a modest rate, yet there are concerns over the recovery pace.

High unemployment rate – which stayed on average at 8.2% in Q2 – was a major concern for US policy-makers. In a bid to rev-up the market, the Federal Reserve expanded its "Operation Twist" bond swapping program by $267 billion. The programme, originally set to expire at end-June would now run through 2012. It would entail the Fed selling short term securities with maturities of approximately 3 years or less. These funds would be used to buy longer-term instruments spanning between 6-30 years. The action is expected to ease the credit market constraints and keep interest rates as low as possible. The Fed reiterated its view that economic slack may warrant "exceptionally low" interest rates through at least late-2014 as inflation remains in check. For the rest of 2012, there are worries that growth could stall due to excessive fiscal tightening caused by political gridlock. Overall growth for 2012 is shaved down to a range of 1.9% to 2.4% from 2.4% to 2.9%.

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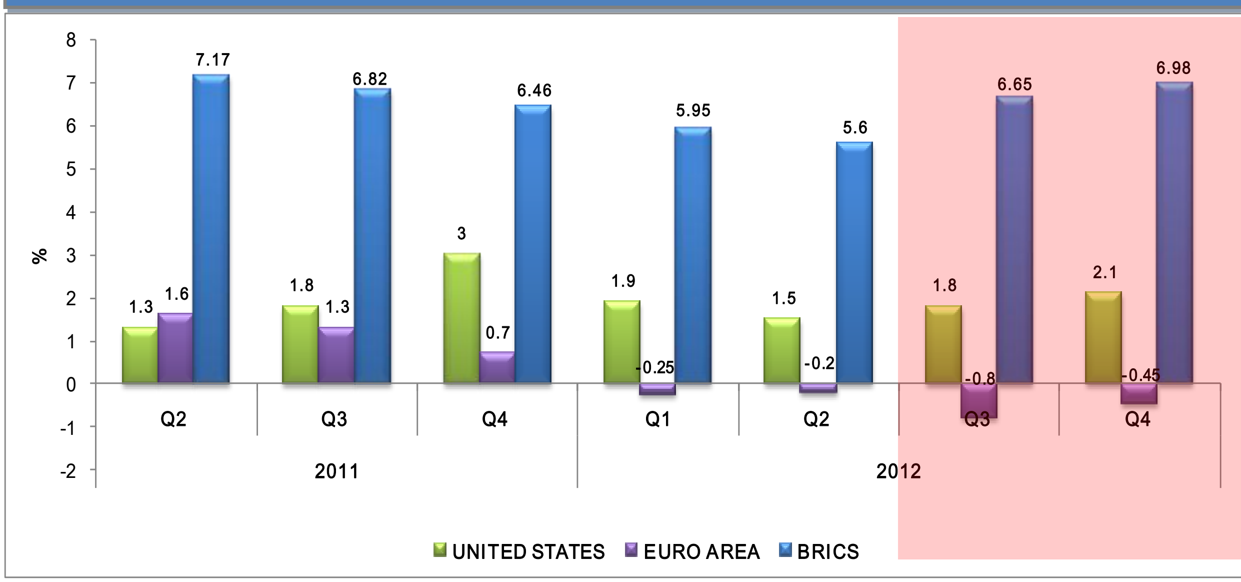
1.2 Euro Area

The Euro area – particularly the Eurozone economies – received the most attention in Q2 2012. GDP in the region contracted by 0.2% in Q2 from zero growth recorded in Q1. The single-currency area's largest economy – Germany – saw its GDP grow 0.3% in the Q2, slower than the 0.5% increase in Q1 but better than forecast. Worries that Germany will succumb to the regional crisis did not materialize as the economy continued to produce positive GDP prints. The economic volume of France, 2nd largest economy in the Eurozone, was unchanged in Q2, the third consecutive quarter for the country's economy to stagnate. Italy's economy shrank by 0.7% from April to June after a 0.8% quarter-on-quarter downfall in the first three months this year. Growth in Spain, Eurozone's fourth largest economy, continued the downward trend seen in previous two quarters with growth decelerating by 0.4%. Figures from Eurostat, the bloc's number-crunching body, also showed that the economy of heavily-indebted Greece further shrank by 6.2% in Q2 compared with a year ago, after contracting 6.5% in the previous month. Britain, EU's second largest economy, registered a 0.7% growth contraction.

GDP Growth Rate & Forecasts – Regional Comparison



Source: Bloomberg & IMF

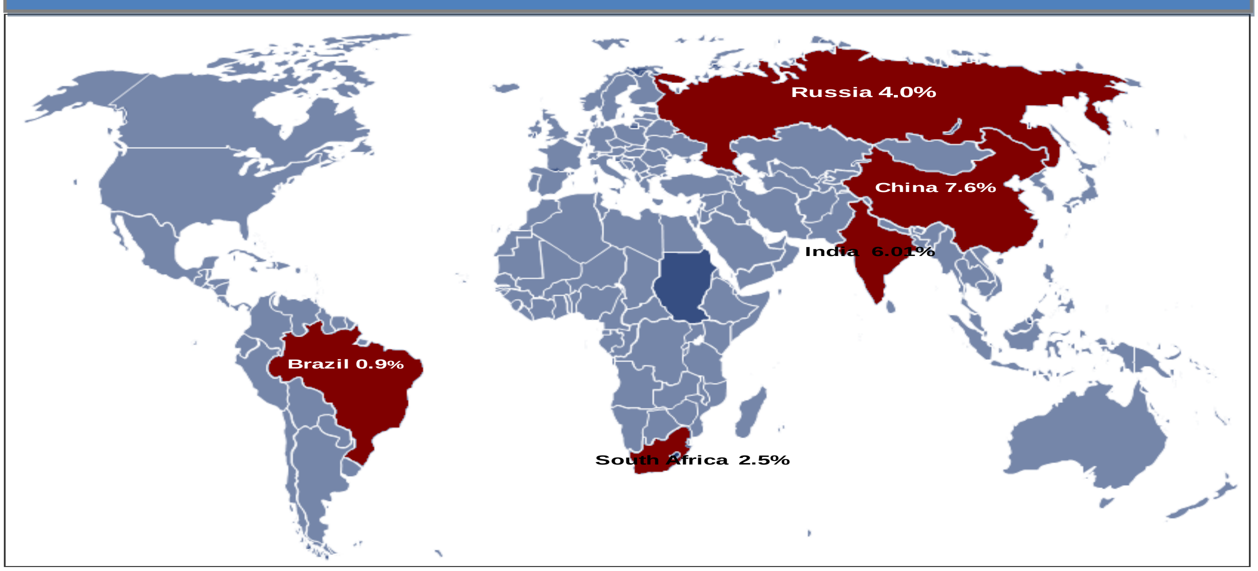
At the heart of the zone's problem is the recurring debt crisis and search for credible solutions. After 18 disappointing Summits, Europe leaders agreed to what appears to be a lasting solution. Ailing banks would be recapitalized with funds intended to bail out indebted governments – a move to "break the vicious circle" of bank bailouts, piling debt on already stressed sovereigns. An agreement was also reached to establish a united supervisory mechanism for euro-zone banks as well as a long-term framework toward tighter budgetary and political union. European Union leaders also agreed to a growth package worth €120 billion to create jobs and encourage growth. This comes after surging borrowing costs and ensuing debts crisis stirred up concerns over possible collapse of the currency union which risk damaging the global economy.

Nevertheless, skepticisms exist whether the moves will be enough to fix Europe's debt crisis, especially as the amount of money available to help in the crisis — some €500 billion — is dwarfed by the amount of debt across the continent. Italy alone has outstanding debt of €2.4 trillion. The European Central Bank (ECB) concerned about the economic health of the periphery economies left its main interest rate at 1%. The region that generates about 16% of the world's economic output may continue to struggle to put its two-year debt saga behind it.

1.3 BRICS

Emerging economies, notably China, Russia, India Brazil and South Africa – which combine as the biggest marginal generators of global output recorded anemic growth. Output expansion in BRICS economies was 5.6% in Q2 2012 down from 7.17% reached in the corresponding period last year.

Q2 2012 GDP Growth: BRICS



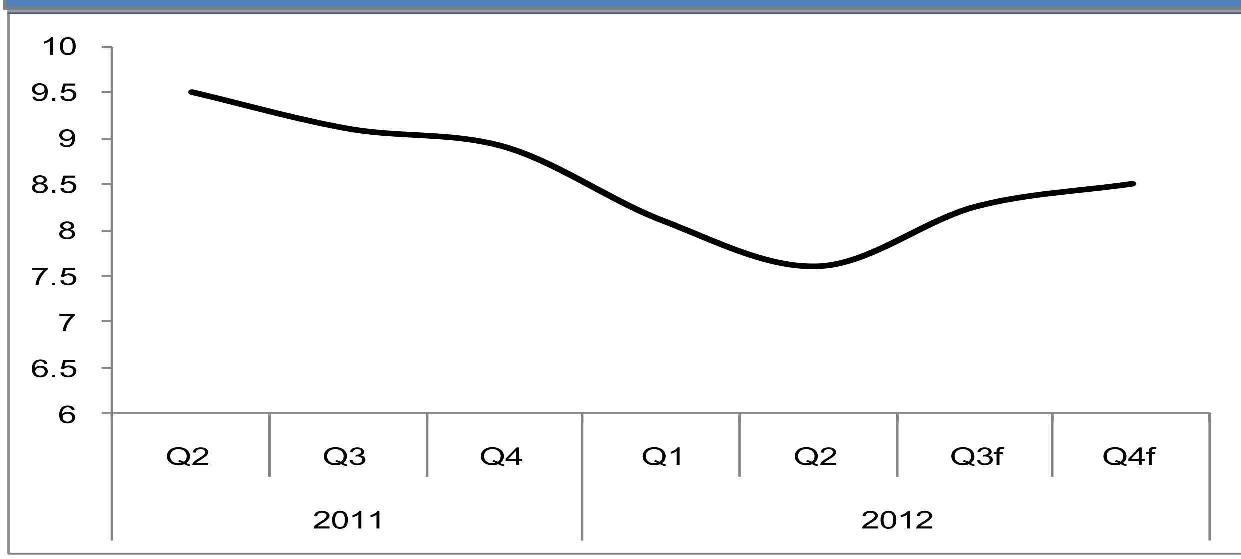
Source: Bloomberg

This partly reflected a weaker external environment. Drop in domestic demand in response to capacity constraints and policy tightening was the other reason. Many emerging market economies were hit by increases in investor risk aversion and perceived growth uncertainty. This led not only to equity price declines, but also to capital outflows and currency depreciation. Whilst many of the concerned countries still have time for monetary easing to respond to large adverse shocks (domestic or external), fiscal stimulus remains a second line of defence.

China

In China, GDP grew by 7.6% in Q2 from a year earlier – slowest pace in 3 years. The world's 2nd largest economy grew at an annual rate of 8.1% in Q1. In an attempt to boost its slowing growth, China – during the quarter – lowered its key interest rate for the first time since 2008. The benchmark one-year loan rate was cut by 25 basis points to 6.31% while deposit rates were reduced to 3.25% from 3.5%. The People's Bank of China also gave banks more room to offer higher rates to savers and lower rates to borrowers. The rate cut is expected to help boost Beijing's domestic economy following diminishing export demand from Europe.

GDP Growth Rate & Forecast – China



Source: Bloomberg

Portfolio investments that can be injected into Beijing's economy were also raised to $80billion from $50billion. By this action, the government hoped to increase investment and competition in its financial and banking sectors. To bolster the economy, Beijing also cut the amount of cash banks are required to hold as reserves – reserve requirement ratio (RRR) – three times since November 2011, and twice in three months this year. Despite inflation falling below the government's 4% target in April 2012, the World Bank expects China's economic growth to ease to 8.2% in 2012 from 9.2% in 2011.

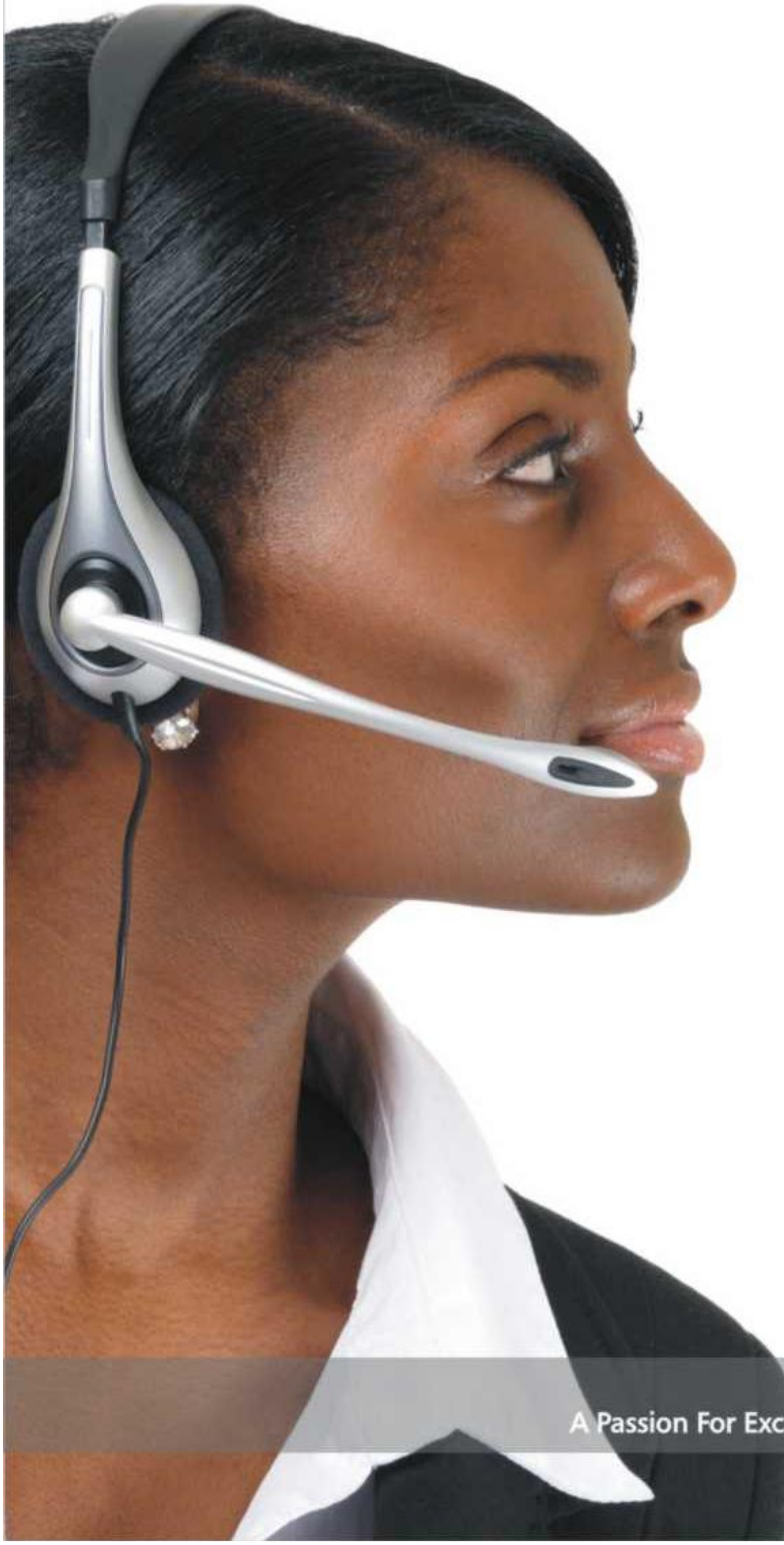
India

Estimates of GDP in India puts growth at about 6.01% in Q2, almost 2 percentage points lower than 8% attained 12 months ago. The Reserve Bank of India (RBI) raised its benchmark interest rate by 50 basis points to 7.25% from 6.75% during its Monetary Policy Committee (MPC) meeting in the quarter. The increase – 9th since March 2010 – was hinged on the need to balance the upside risk to price stability and downside risk to GDP growth. Inflation remained persistent due to increase in energy and food prices. IMF projects that India's GDP growth would decline to 6.1% in 2012 from 7.1% growth recorded in 2011. RBI also increased the savings deposit rate to 4% from 3.5% in a bid to make the window attractive to stem inflationary monetary growth.

GDP Growth Rate & Forecast – India

Source: Bloomberg & IMF

»» FEEDBACK OR CONCERNS?



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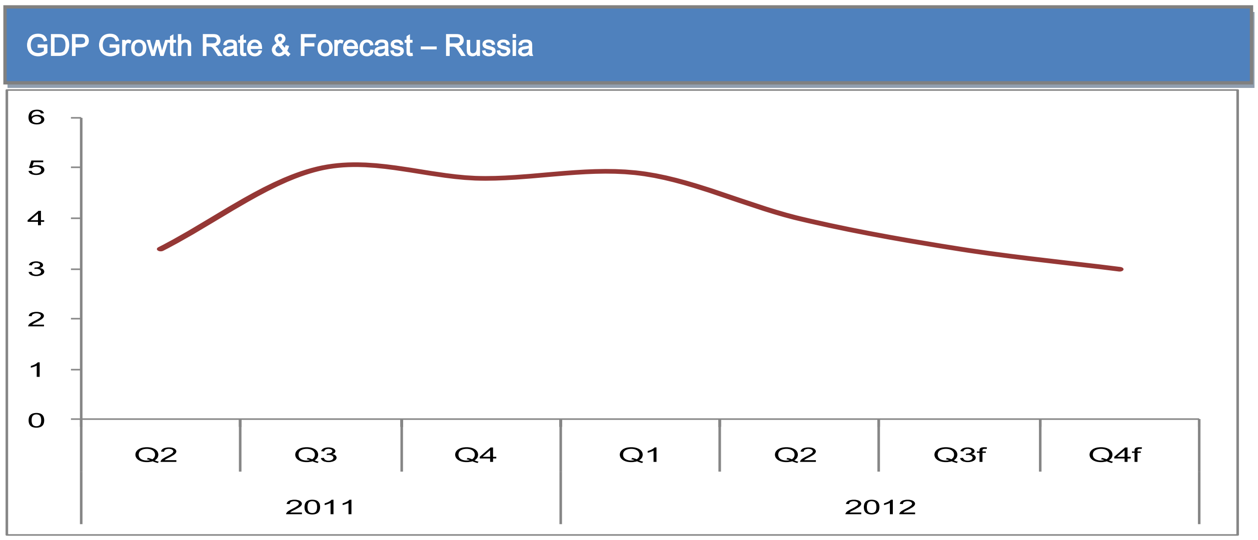
Russia

Russia's GDP movement bucked the trend. Moscow's Q2 2012 GDP growth was up 60 basis points to 4% from 3.4% in Q1 2011. The strength of the Russian economy results from robust domestic demand, reinforced by unemployment falling back to the pre-crisis level of 5.8%.



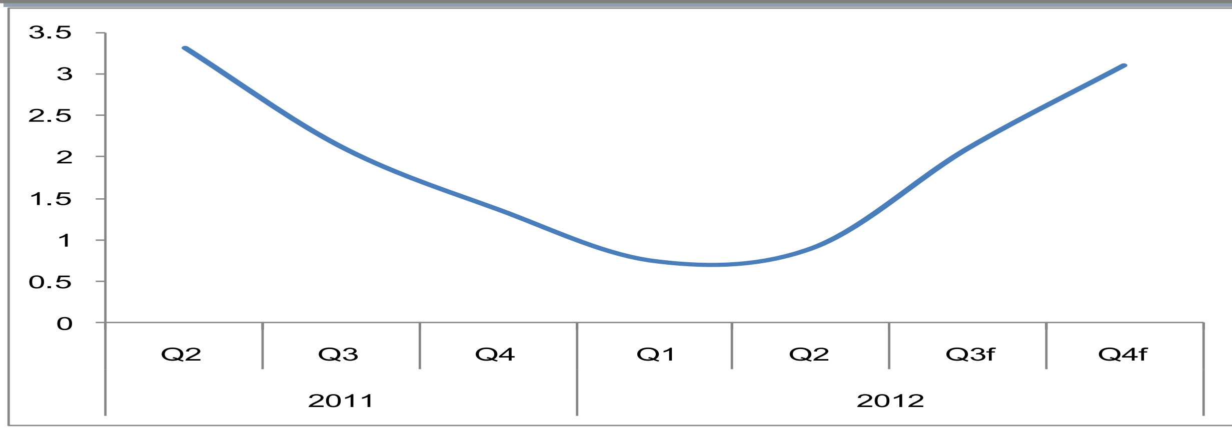
Source: Bloomberg & IMF

This aided fast wage growth, as well as rapid expansion of credit to households. Comparing growth Q-on-Q, GDP dropped by 90 basis points from Q1 2012 figure.

Brazil

Despite disappointing industrial output and net job creation, Brazil's GDP grew 0.9% in Q2, 15 basis points higher than the figure for Q1. A 15% weakening of the Brazilian Real since March boosted the profitability of its commodity export buoying growth.

GDP Growth Rate & Forecast – Brazil



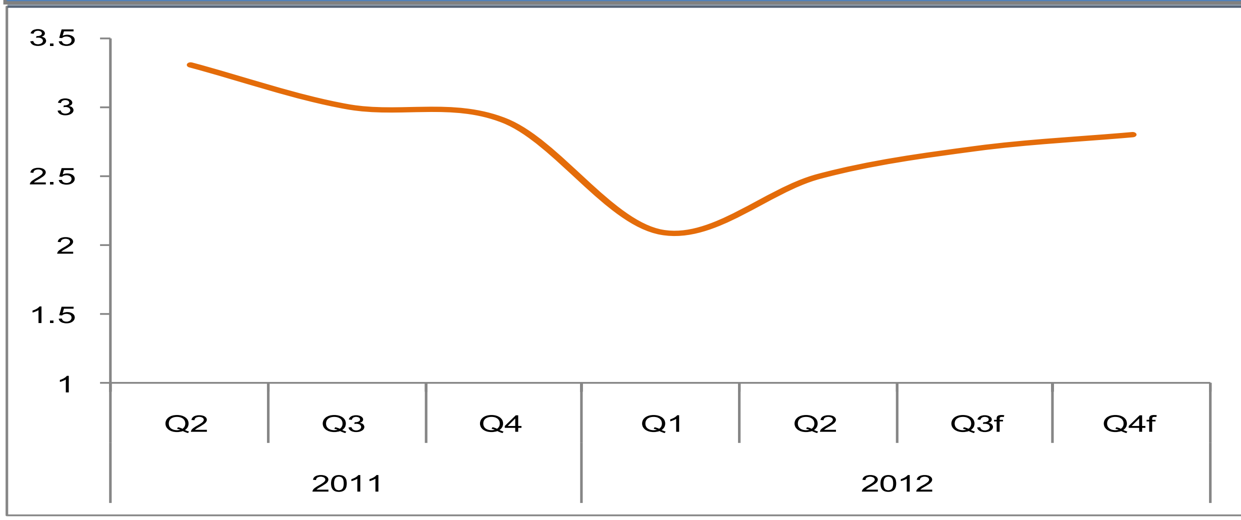
Source: Bloomberg & IMF

On the inflation angle, disinflationary local and global conditions eased Brazil's annual inflation rate to 4.92% in June. Inflation is expected to remain around these levels until stimulus measures boost demand and aggregate prices. Pessimism over the prospects of Latin America's largest economy has raised urgency within the government for new measures to cut costs and spur investments. Growth in the world's 7th largest economy was revised down to 1.81% in 2012 from 1.85% previously – a far cry from the 7.5% boom seen in 2010. Growth headwinds include weaker conditions in developed markets and China, and a hard landing in neighbouring Argentina (Brazil's third-largest market and an important destination for its manufactures, especially cars).

South Africa

South African's GDP expanded at a slower pace of 2.5% in Q2 2012 lower than the 3.3% growth recorded in the corresponding period last year. Growth moderated in Africa's biggest economy due to weak external conditions and global uncertainty. The stubbornly high unemployment rate – about 25% – also contributed to the weak growth.

GDP Growth Rate & Forecast – South Africa



Source: Bloomberg & IMF

IMF projects GDP growth will likely reach 2.6% in 2012 lower than 2.7% earlier estimated. The rising level of government debt coupled with the budget deficit also suggests a declining fiscal space to cope with future shocks.

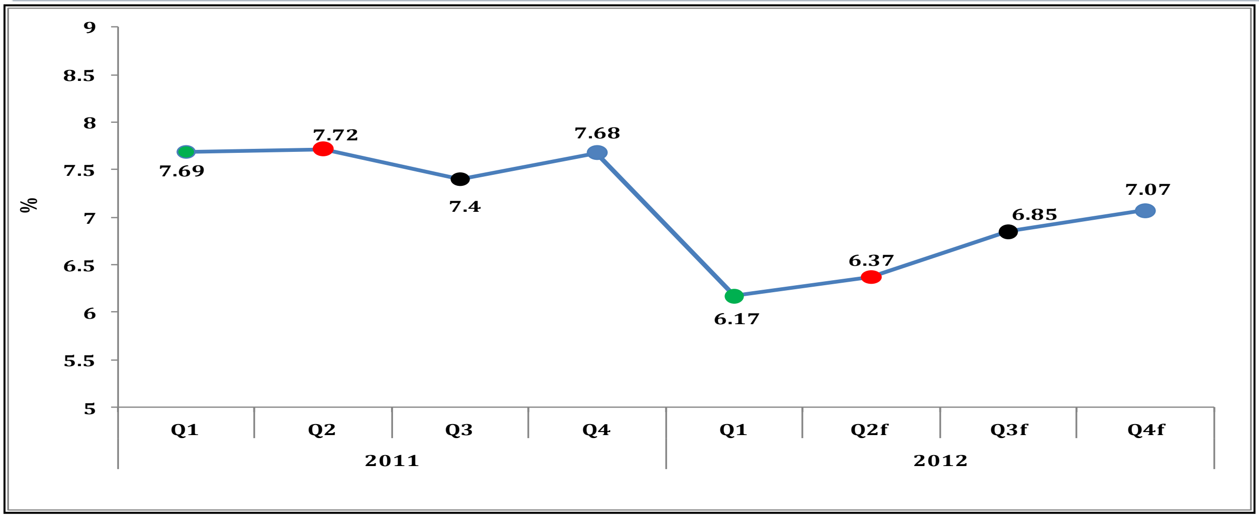
2.0 The Nigerian Economy

Below is a summary of other defining characteristics of the economy in Q2 2012.

2.1 GDP Growth

In spite of the decline in economic activity in Q1 – following the partial removal of fuel-subsidy and weaker consumer demand – output expansion gathered traction in Q2 2012. Gross Domestic Product (GDP) is estimated to have grown by 6.37% in Q2 lower than the 7.72% recorded in the corresponding quarter of 2011. The GDP growth print was 20 basis points higher than the 6.17% recorded in the preceding quarter. The Q-on-Q increase stems from growth coming from the non-oil sector – which has continued to contribute more to the nation's GDP 'pie'. The non-oil sector is expected to remain a growth-driver for the remaining half year.

GDP Growth Rate



Source: NBS

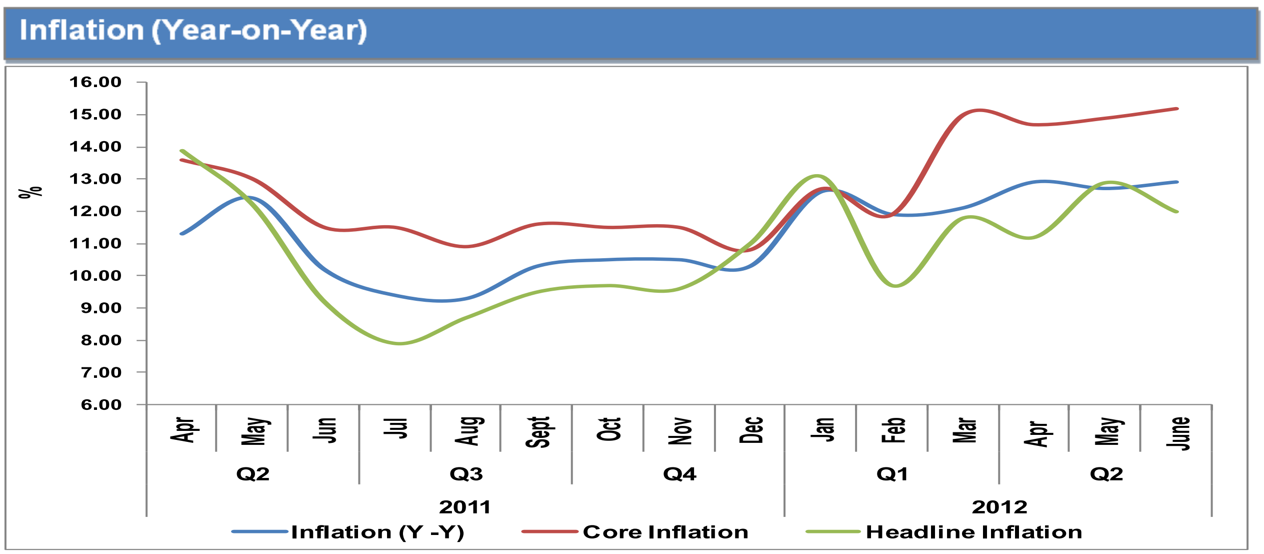
In Q3, the nation's global GDP position may likely see a significant upswing. This follows the intended plans to change the GDP base year to 2008 from 1990. This would increase Nigeria's GDP stock by 40% to about $579 billion from $414 billion as at 2011. By implication, Nigeria is projected to overtake South Africa and become the continent's largest economy by 2017.

2.2 Inflation

There was diminutive movement in the inflation figure in the review period as inflation lingered around the 12.7% – 12.9%. June inflation figure was up 20 basis points to 12.9% from 12.7% recorded in May. Inflation in April stood at 12.9%.

Core inflation components, particularly higher transport costs, contributed more to inflation in the quarter. It rose from 14.7% to 14.9% between April and May. It edged further to 15.2% in June.

Headline inflation however, exhibited mild volatility. It dropped to 12% in June from 12.9% in May. It was 11.2% in April. Increase in prices of some farm produce such as yam tubers, non-food items and abrupt rise in electricity tariff were headline inflation drivers.



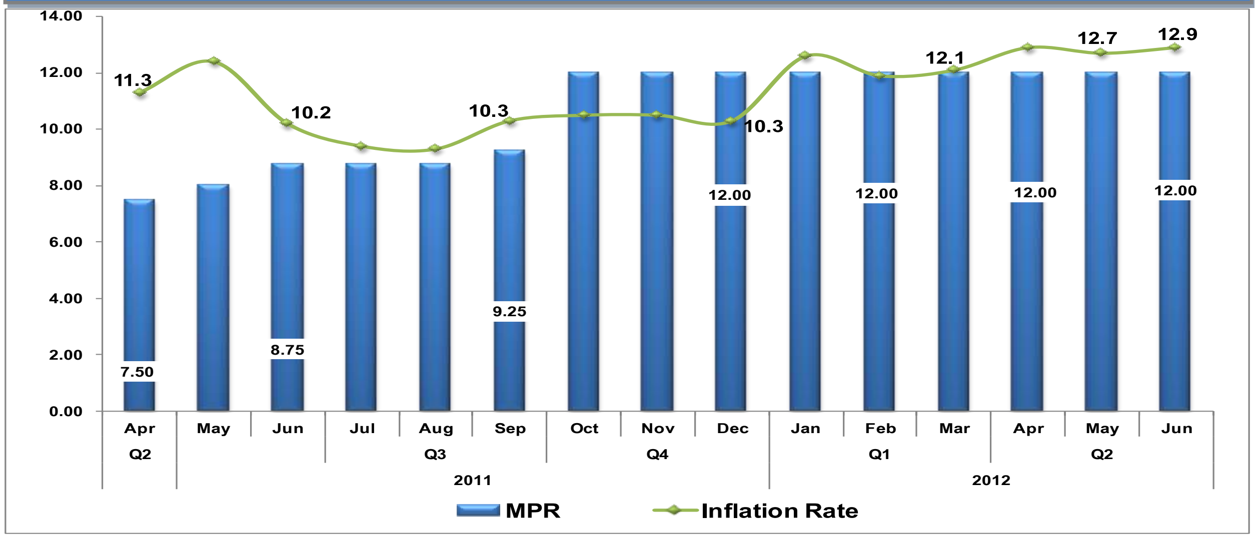
Source: NBS

For Q3 2012, inflation expectations remain high owing to increase in power tariffs and 2012 budget spending.

2.3 Monetary Policy

The Central Bank of Nigeria (CBN) at its only Monetary Policy Committee (MPC) Meeting held in Q2 maintained policy status quo – MPR retained at 12%. This was to ensure price stability, sustain foreign investment inflows and promote exchange rate stability. The MPR has remained unchanged since October 2011 – when it was raised by 275 basis points from 9.25%. The banking regulator, during the quarter, also actively used Open Market Operations (OMO) to mop up excess liquidity from the banking system. Total amount withdrawn in the period was about N681.42 billion as against N1.04 trillion in Q1. Monetary policy outlook for Q3 2012 is likely to focus on stabilising the Naira while ensuring inflation is put in check.

MPR and Inflation

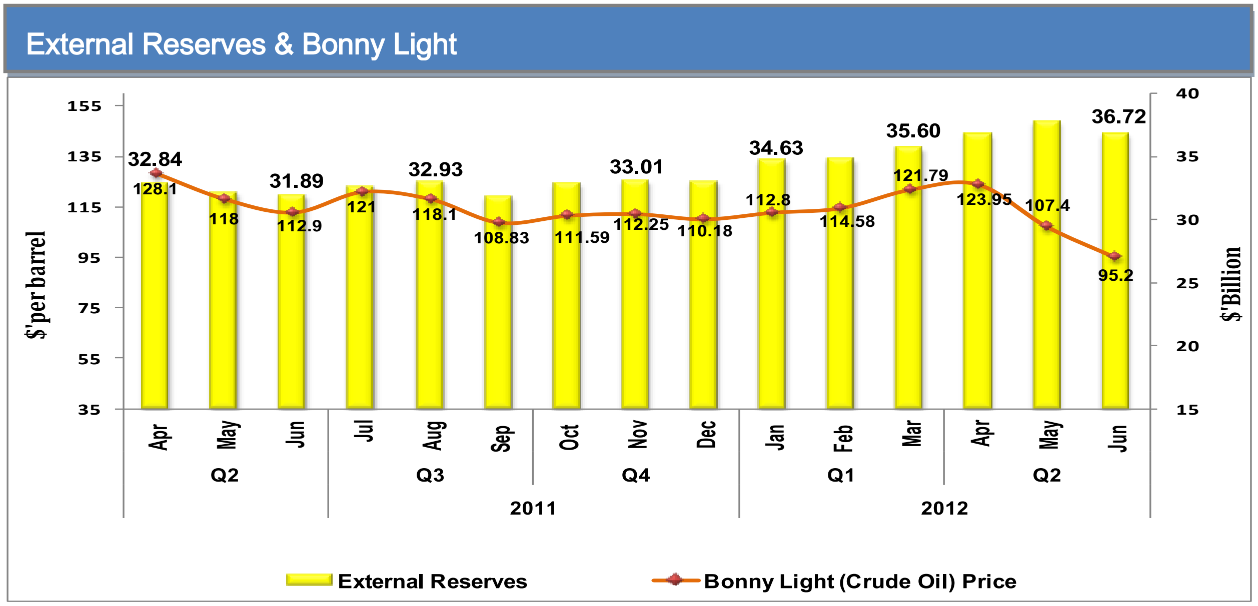


Source: NBS

2.4 External Reserves

Steady rise in external reserves and a pressured Naira were major phenomena in Q2 2012. External reserves rose to US$36.72 billion as at end-Q2 from US$35.6 billion in Q1 – an increase of 3.15% or US$1.12 billion. The reduction in government's financial burden – following the partial removal of subsidy on petrol – helped accretion to the 'foreign currency pot'. Favourable international crude oil prices and fund inflows by offshore investors in response to the relatively high domestic interest rates aided the nation's savings drive.

Foreign exchange reserves reached a quarter high of US$37.76 billion on June 6, 2012 – highest level in 22 months, but declined thereafter. The drop was due to huge demand on the reserves by banks to meet dollar obligations. Nigeria's external reserves have remained resilient over $30 billion with downside risk to its growth on the rise – particularly from volatile oil price movements.



Source: CBN & FMDA

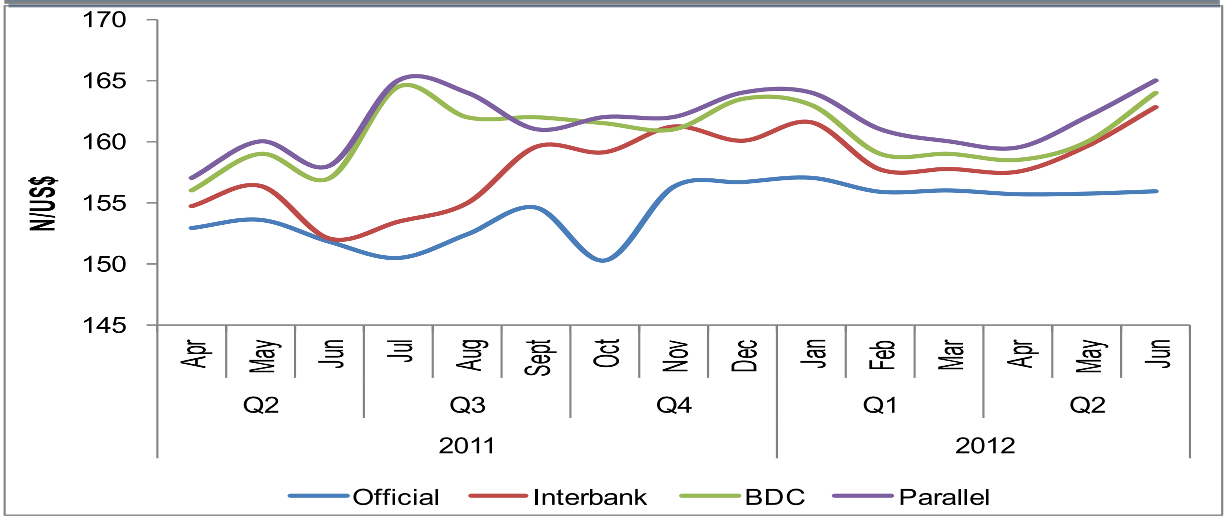
2.5 Exchange Rate

At the foreign exchange market, Naira remained within the indicative N155/$±3% target in Q2. It marginally strengthened against the US Dollar at the CBN window – helped by prudent monetary policy adopted by the apex bank. It weakened at the interbank market due to demand for the greenback by corporate institution and oil importers. Low dollar sales by oil companies coupled with capital repatriation activities by offshore investors exiting bonds holding reduced dollar liquidity at that market segment.

The banking regulator maintained a target band of between N150/US$ and N160/US$, at the official window. The Naira/Dollar exchange rate at the CBN window closed at N155.94/US$ on June 29, 2012 after opening Q2 2012 at N156.01/US$, gaining 7 kobo.

However, interbank rate movements were more volatile. It rose from N157.59/US$ on April 2, 2012 to N163.21/US$ on June 15, 2012 – a development that might have crossed the N164/US$ level in a few weeks if CBN had failed to sustain its direct sales to the interbank market. It closed the quarter at N162.85/US$ – a Q-on-Q depreciation of 3.2%. Total CBN Dollar sales in the quarter were $5.39 billion as against $4.57 billion in the preceding quarter.

Exchange Rates



Source: CBN & FMDA

The local currency may sustain recent stability levels on the strength of CBN avowed commitment to keep Naira at current band i.e. N155/US$ +/- 3%. However, significant risks to exchange rate outlook stems from declining external reserves due to volatility in crude oil price and slowdown in output amid fragile pace of global economic recovery.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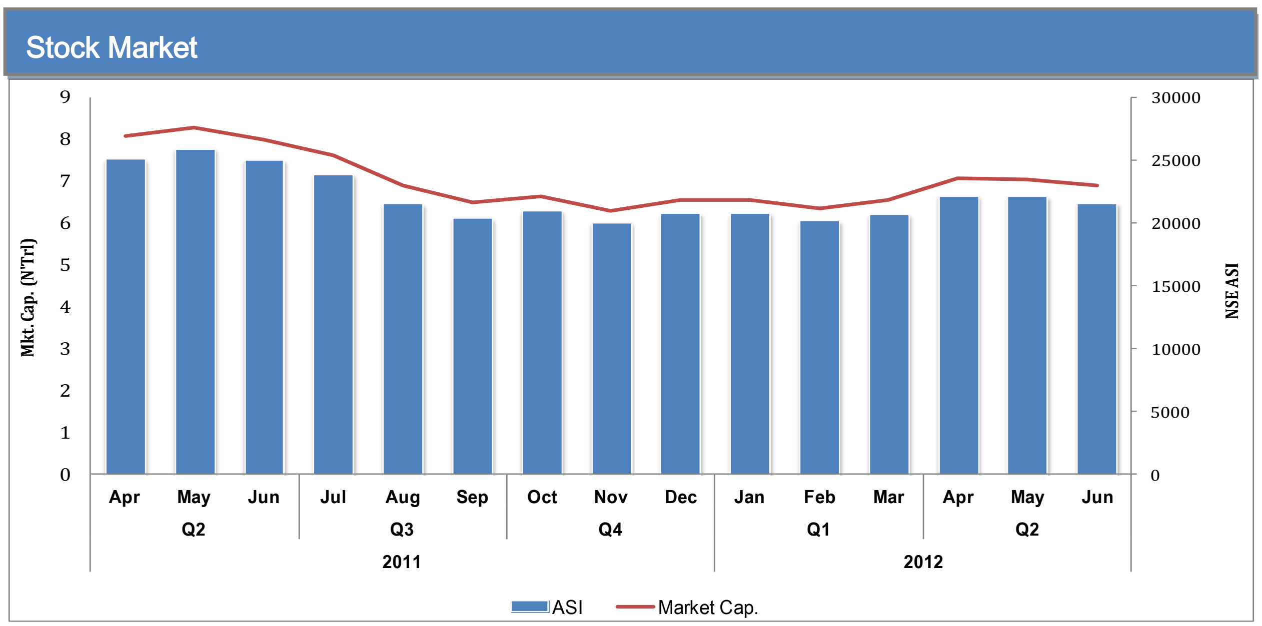
2.6 Stock Market

Performance indicators at the bourse closed higher in the review period as bargain activities outweighed sell pressures on renewed optimism for equities. The Nigerian Stock Exchange All Share Index (NSE ASI) rose by 4.31% to 21,542.24 points in Q2 2012 from 20,652.47 recorded in Q1. Similarly, market capitalisation gained N327 billion to close at N6.87 trillion. It topped the N7 trillion mark in the quarter – last achieved 8 months earlier – reaching N7.23 trillion on May 4. The uptick was adduced to encouraging Q1 2012 scorecards released by sectoral bellwether companies – Banking and Fast Moving Consumer Goods.

Increased foreign capital inflows also contributed to market trend observed as recent reforms embarked upon by Securities & Exchange Commission (SEC) helped to restore market confidence. Year-to-date performance on the index at close of Q2 was 3.92%.



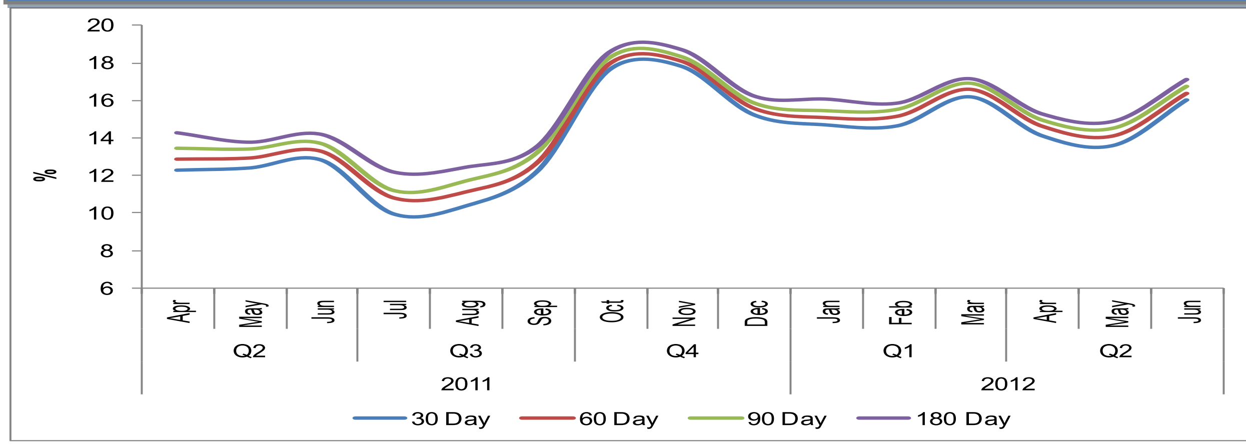
Source: NSE

The bullish run may likely continue in Q3 given expected financial reports by some bluechip companies coupled with attractive dividend payouts.

2.7 Interbank Interest Rates

Interbank rates surprisingly trended downwards despite CBN's monetary tightening stance to manage inflation. Overnight and call rates closed at 15.45% and 15.08% from quarter-start figures of 15.55% and 15.75%, in that order. Similarly, 90-day interbank lending rate dropped to 16.76% from 16.93% in Q1. Statutory inflows maintained the customary role of being rate-drivers in the market.

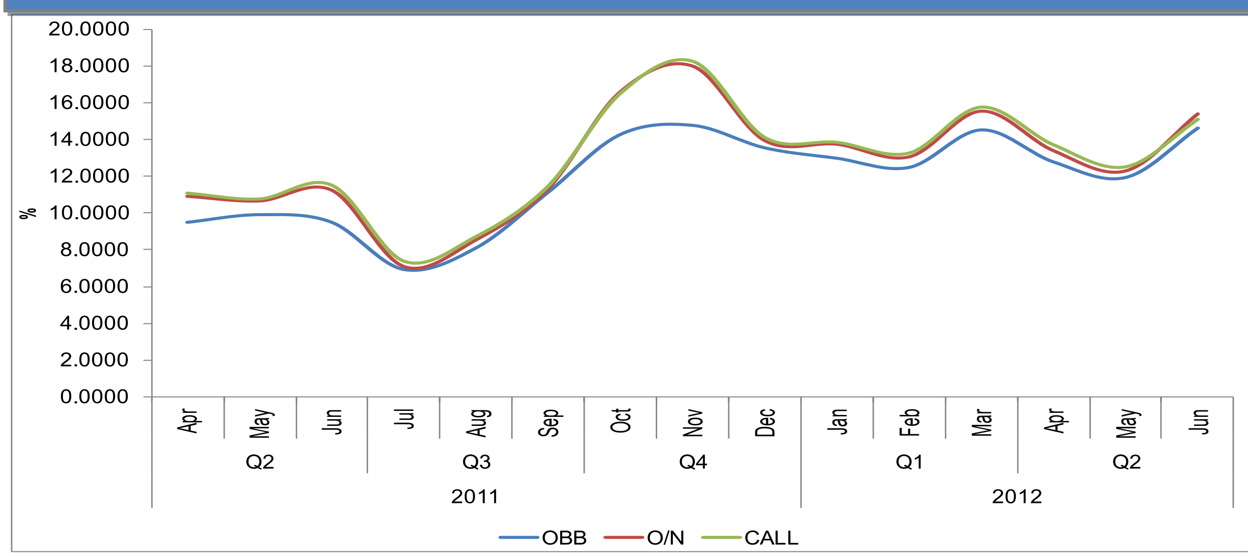
NIBOR



Source: FMDA

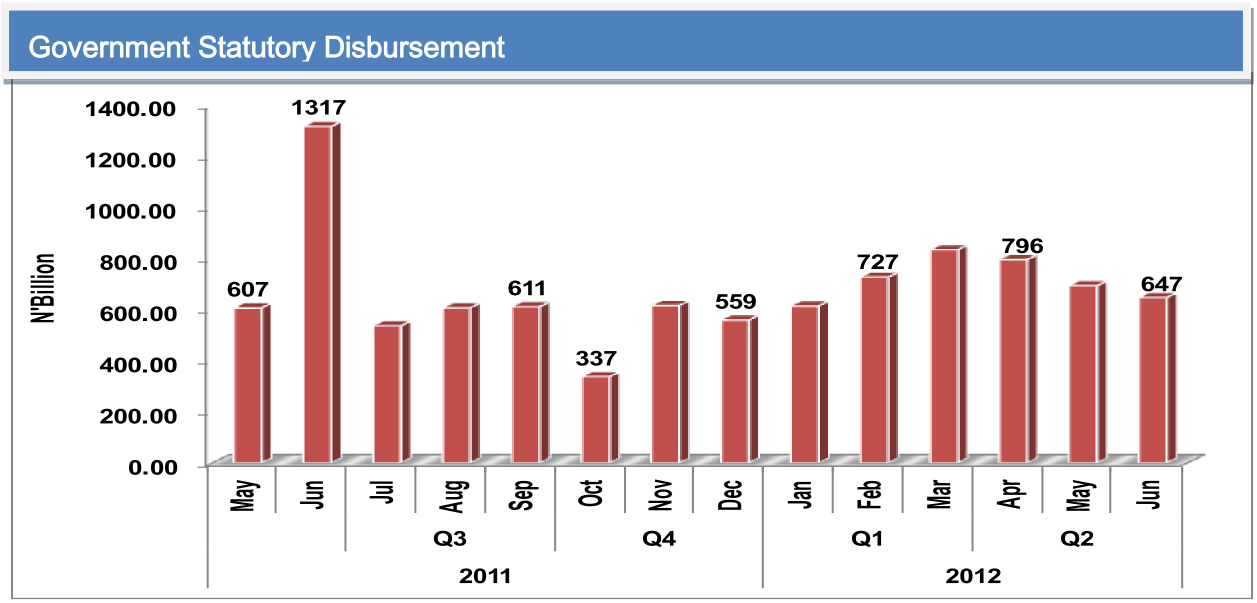
Disbursements of statutory allocation by the Federation Account Allocation Committee (FAAC) were N2.14 trillion – 10% higher than the N2.38 trillion distributed in the previous quarter. Nigeria's financial institutions rely on statutory allocation for a significant chunk of its liquidity – which often dictates the directions of bond yields and interbank rates.

NIBOR – OBB, Overnight $ Call Rates



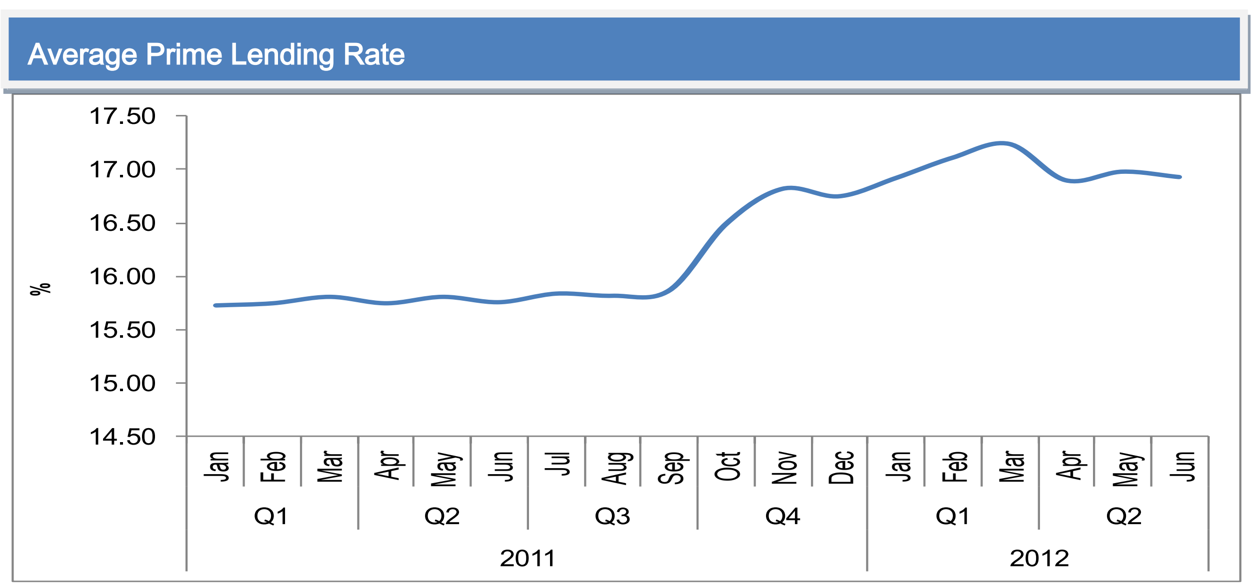
Source: FMDA

Other systemic funding sources in the quarter include maturing treasury bills of over N900 billion coupled with N250 billion in bond payments



Source: Budget Office & FMDA

On average, prime lending rate of Deposit Money Banks (DMBs) slightly declined to 16.93% in Q2 2012 down from 17.28% in Q1. This may have been induced by relatively low cost of funds. Lending rates are projected to maintain an upward trajectory given CBN's tightening monetary policy.



Source: CBN

2.8 Financial Sector

The Central Bank of Nigeria (CBN) embarked upon a number of initiatives in the quarter. Policies aimed at ensuring stability of the financial system, increasing financial services penetration and enhancing the 'cashless' scheme received the regulatory authority attention.

The CBN put in place measures to adopt a risk-based supervision and macro-prudential framework for banks – a move to further stabilize the Nigerian financial sector. Part of the framework entails the creation of a credit risk officers' forum, to serve as a body to discuss issues and proffer solutions to emerging risk issues. The proposed risk framework would encourage banks to embrace a holistic approach towards risk management in financial institutions, especially in mitigating against banks failing. This enterprise-wide approach to risk management would also help financial institutions change their perception about risk management and channel resources towards averting risks in the system.

CBN also developed a draft on financial inclusion strategy in order to improve the percentage of Nigerians with bank accounts. The strategy is aimed at reducing the percentage of adult Nigerians excluded from financial services to 20% by 2020.

CBN further made known its plans to soon commence another Know-Your-Customer (KYC) exercise for banks in the country. The move is aimed at adopting the new National Identity Number (NIN) (issuance to start September 1, 2012) as the new KYC requirement for financial transactions. In 2011, the CBN compelled bank customers to update their details through submission of passport photographs, utility bills and current residential addresses. The new Initiative would primarily capture customer's biometrics, issuing them the NINs and the General Multi-Purpose Card (GMPC). During the exercise, customers would also be provided with verification "infrastructure" for linking their accounts to the issued NIN. Effective January 8 2013, the NIN would be the basis for KYC verification and compliance by all deposit money banks.

In Q2, the banking regulator directed all banks in Nigeria to allow new customers open account with zero amount – a move to make banking services accessible to the unbanked. The new policy compels banks to adopt only the reducing balance method in calculating interest charges on loan repayment (in instalments), as other methods would result in the payment of higher effective interest rates. The policy statement further goes on to stop the ceiling placed on savings account closing balance and minimum opening balance of new accounts. It is expected that the initiative, if fully implemented, would stimulate economic growth as the unbanked public would be attracted to banking services while banks develop new products to improve access to credit.

In a separate development, the Central Bank of Nigeria (CBN) released guidelines for the truncation of cheques by banks to further enhance payment system efficiency in the country. Cheque truncation is a process that involves the use of instrument images and the corresponding data contained in Magnetic Ink Character Recognition (MICR) line for clearing purposes. This is to replace the use of physical instrument as it is currently practised. The planned cheque truncation regime would ensure that cheques are cleared on a T+1 basis such that customers receive value in the morning of the second day. According to the regulator, the policy is aimed at reducing the period (time) and cost (amount) it takes in clearing an instrument and articulates the rights and responsibilities of both the presenting and paying banks. It would also provide for minimum technical and operational standards.

3.1 Outlook for Q3 2012

Macroeconomic environment will likely be characterized by:

- GDP growth to stay over 6.2% in Q3 2012;
- Depreciation in inter-bank FX rate may moderate – recent policy interventions of the CBN have reduced demand pressure. FX at CBN window would likely remain within the N155/$±3% target
- Inflation may continue with its up-trend given rise in energy tariff and increased spending from Budget 2012;
- Stock Market – Upward momentum anticipated. However, downside risk remain decline in investible funds.
- Weak global demand and tempered outlook mean energy prices may witness a slowdown, possibly helping growth recovery efforts in the U.S. Still, global capital flows may continue to migrate to more promising climes like Nigeria helping the Naira and buoying growth.

3.2 Factors to shape the Market in Q3 2012

- To focused on liquidity tightening
- Government spending from 2012 Budget
- Informed and planned regulatory reforms
- More Initiatives at reducing poverty and creating jobs
- Cashless Economy: Gaining momentum
- Security challenges in the Northern states and the Niger Delta
- Growth concerns from world's richest economies and lingering debt crisis in the Eurozone.

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