CORONATION

Coronation Economic Note

11 February '22

The thoughts of IMF via its Article IV on Nigeria

Today we shed some light on the recently published IMF Article IV on Nigeria. The consultations with Nigerian officials on economic developments and policies for the 2022 Article IV ended in mid-November. The publication commends the authorities for the measures taken to address the health and economic impacts of the COVID-19 pandemic which have exacerbated pre-existing weaknesses. However, it emphasised the need for major reforms in the fiscal, exchange rate, trade, and governance areas to support long-term, inclusive growth and sustain macroeconomic stability.

For national output, the Fund projects a GDP growth of 2.7% for 2022. Non-oil growth is projected to broaden but remain sluggish due to inward looking policies and the infrastructure gap among others. However, oil production is expected to increase gradually but remain below the 2019 level. Our estimate for GDP growth this year is 2.6%.

According to the IMF, the projected outlook faces balanced risks. On the downside, low vaccination rates expose Nigeria to future pandemic waves and new variants, higher debt service to government revenues (through higher US interest rates and increased borrowing) poses risks for fiscal sustainability. However, some potential positives include: boost to non-oil growth on the back of supportive credit policies, rebound in oil production, supported by the terms in the Petroleum Industry Act and benefits from Nigeria's ratification of the African Continental Free Trade Area (AfCFTA) agreement.

Based on the report, in the short run, a consistent macroeconomic policy mix, supported by a comprehensive capacity development strategy is required to ensure robust recovery in growth. Furthermore, a supportive monetary policy remains appropriate for now, but a gradual tightening will be required to reduce structurally high inflation. Looking ahead, better monetary transmission mechanisms as well as deeper trade reforms are required to enhance macroeconomic stability. In our view, revenue mobilization should also feature in the priority list.

Given the limited policy space and continued dependence on central bank financing, fiscal consolidation is essential. IMF staff recommended a few measures which could result in net savings of 5.1%of GDP between 2022 – 2026. They include; keeping the public debt-to-GDP ratio below 40%, reducing government interest payments-to-revenue ratios, and creating room for additional social assistance.

The report welcomed the removal of the official exchange rate but highlighted that the premiums in the parallel market and the bureau de change (BDCs) exchange rates have stayed elevated and widened further following the authorities' decision to discontinue fx supply to the BDCs in July '21. The IMF recommended that the authorities consider further measures that could result in a unified and market-clearing exchange rate.

Indicators	NG
Inflation rate (December '21, %)	15.63
GDP (Q3 '21, %)	4.03
Gross Official Reserves (10 February '22, USD bn)	39.9
UK Brent (11 February '22, USD)	91.9

Source: Bloomberg, CBN, NBS, Coronation MB Research

FGN bond yields (11 February '22, %)			
14.20%	13.98%	12.15%	12.40%
Mar-24	Feb-28	Jul-34	Mar-36
8.29	12.00	12.57	12.81

T-bill yields (11 February '22, %)			
31-Mar-22	30-Jun-22	29-Sep-22	24-Nov-22
2.01	4.30	5.38	5.10

Source: FMDQ, Coronation MB Research

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We note that a clear exchange rate policy would help attract larger capital inflows, including foreign direct investments, which have significantly dropped in recent years.

Regarding tax measures, the IMF encourages the authorities to adopt tax rates comparable to Nigeria's peers in the Economic Community of West African States (ECOWAS). These include further increasing the VAT rate to at least 10% by 2022 and aligning the VAT rate with the ECOWAS average of 15% by 2026. An additional recommended measure is increasing the excise rates on alcoholic and tobacco products combined with a broadening of the base.

The report stressed the importance of well-targeted and adequate social policies. Despite recent improvements, for example, adding one million households to the social registry, Nigeria's social safety net still suffers from limited coverage and weak targeting. The IMF recommends increasing social spending by up to 1% of GDP cumulatively between 2022-2026 (c.0.2% of total GDP each year). The newly launched eNaira could help foster financial inclusion and improve the delivery of social assistance. However, close monitoring of associated risks is important.

The report noted that the ratification of the AfCFTA holds huge prospects for job-rich growth through regional trade and economic integration. However, bold reforms are needed to allow Nigeria to maximize its gains from the AfCFTA. Streamlining import documentation requirements and reducing customs clearance time; improving the customs capacity to enforce preferential rules of origin and keeping land borders open while addressing smuggling concerns through stepped-up customs reform were a few recommendations put forward by the IMF.

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