Nigeria's operating landscape

December 2017
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Economic Context
Five global themes to consider in 2018

1. Brexit & European instability
2. Trump’s protectionist stance
3. Monetary Policy tightening in key advanced economies
4. Unrest in the Middle East
5. Phasing out of oil
Nigeria is the largest economy in Africa. However, growth has fallen sharply since 2010, with the economy falling into recession in 2016 due to an oil-induced crisis.

Top 5 Africa Economies by 2016 (Nominal GDP)

1. Nigeria - $405.0Bn
2. Egypt - $336.0Bn
3. South Africa - $314.7Bn
4. Algeria - $156.1Bn
5. Morocco - $101.4Bn

Annual Real GDP Growth (%)

Average growth: 4.6% (2010-2016)

Source: IMF World Economic Outlook October 2014, World Bank
Nigeria's operating landscape • 2018 Budget
With a quickly-expanding population, technology adoption and rising investment, by 2050 the nation is expected to become the first African nation to become a top 15 global economy.

<table>
<thead>
<tr>
<th>GDP PPP rankings</th>
<th>GDP MER rankings</th>
<th>Country</th>
<th>2016 rankings</th>
<th>GDP at PPP</th>
<th>GDP at MER</th>
<th>2030 rankings</th>
<th>Projected GDP at PPP</th>
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</table>

Note: GDP at PPP is in constant 2016 international $, GDP MER is in US$
A third of the economy is based on primary industries of agriculture, mining and quarrying (which includes the large oil sector)

2016 Real GDP - Industry Split

<table>
<thead>
<tr>
<th>Industry Split</th>
<th>NGN’BN</th>
<th>%</th>
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<tbody>
<tr>
<td>Agriculture</td>
<td>16,607</td>
<td>24%</td>
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<tr>
<td>Trade, Hotels &amp; Food Services</td>
<td>12,288</td>
<td>18%</td>
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<tr>
<td>Transportation &amp; IT</td>
<td>8,814</td>
<td>13%</td>
</tr>
<tr>
<td>Oil &amp; Gas</td>
<td>5,725</td>
<td>9%</td>
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<tr>
<td>Manufacturing</td>
<td>6,302</td>
<td>9%</td>
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<tr>
<td>Real Estate</td>
<td>4,904</td>
<td>7%</td>
</tr>
<tr>
<td>Public Services &amp; Education</td>
<td>3,088</td>
<td>5%</td>
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<tr>
<td>Business services</td>
<td>2,551</td>
<td>4%</td>
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<tr>
<td>Construction</td>
<td>2,521</td>
<td>4%</td>
</tr>
<tr>
<td>Finance &amp; Insurance</td>
<td>2,028</td>
<td>3%</td>
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<tr>
<td>Other Services</td>
<td>2,733</td>
<td>4%</td>
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<tr>
<td>Electricity &amp; Water Services</td>
<td>335</td>
<td>0%</td>
</tr>
<tr>
<td>Other Mining</td>
<td>87</td>
<td>0%</td>
</tr>
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</table>

Source: NBS, PwC Analysis
Note: Sum of sectors may not equal 100% due to rounding

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December 2017
Nigeria’s economy has returned to positive growth in 2017, but the non-oil sector performance remains weak

<table>
<thead>
<tr>
<th>Top performing sectors</th>
<th>Q3’17</th>
<th>Share of GDP</th>
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<tbody>
<tr>
<td>Crude petroleum</td>
<td>25.8% y/y</td>
<td>10.0%</td>
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<tr>
<td>Livestock</td>
<td>4.0% y/y</td>
<td>1.6%</td>
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<tr>
<td>Crop production</td>
<td>3.2% y/y</td>
<td>26.9%</td>
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<tr>
<td>Broadcasting</td>
<td>1.6% y/y</td>
<td>1.2%</td>
</tr>
<tr>
<td>Food, Beverage, Tobacco</td>
<td>0.6% y/y</td>
<td>3.9%</td>
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<table>
<thead>
<tr>
<th>Worst performing sectors</th>
<th>Q3’17</th>
<th>Share of GDP</th>
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</thead>
<tbody>
<tr>
<td>Financial institutions</td>
<td>-6.5% y/y</td>
<td>2.3%</td>
</tr>
<tr>
<td>Road transport</td>
<td>-6.3% y/y</td>
<td>0.9%</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>-5.7% y/y</td>
<td>7.4%</td>
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<tr>
<td>Real estate</td>
<td>-4.1% y/y</td>
<td>6.8%</td>
</tr>
<tr>
<td>Trade</td>
<td>-1.7% y/y</td>
<td>15.9%</td>
</tr>
</tbody>
</table>

- The non-oil sector growth slowed in Q3’17 to -0.76% y/y (Q2’17: 0.5% y/y) – the lowest on record, driven mainly by weak performance in telecommunications, trade, real estate and financial services. However, agriculture expanded 3.06% y/y

- The slowdown in telecommunications deepened to -5.6% y/y in Q3’17 (Q2’17: -1.7% y/y), perhaps reflecting weak telephone and internet subscription (NCC data for August & September)

- Broadly, the contraction in the services sector by -2.6% y/y in Q3’17, the worst on record, is reflective of weak consumer purchasing power

- This suggests that the recovery in the non-oil sector will remain sluggish in the immediate term. However, we expect a modest recovery in 2018, driven by exchange rate stability and increased investment

Source: NBS, PwC Analysis
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Source: National Bureau of Statistics and PwC estimates
Section 2 – Fiscal accounts

Fiscal accounts
Key assumptions of the 2018 budget

- Overall projected budget fiscal deficit of NGN2.0 trillion for 2018, which is about 1.7% of GDP
- The budget deficit is to be financed mainly by borrowings projected at NGN1.70 trillion
- NGN850 billion (50.0% of this borrowing) is intended to be sourced externally, while NGN850 billion will be sourced domestically
- The debt service to revenue ratio is projected to be about 30.5% in FY2018

Financing the deficit

Source: Budget Office, PwC Analysis

*Nigeria's parliament recently adjusted the oil price assumption to U$ 47/bbl in the process of approving the 2018-2020 expenditure framework. This could impact the overall revenue projections, as well as the fiscal deficit for the 2018 budget
2018 budget revenue proposals – Where the money is coming from?

2017 Approved Proposal

- Oil revenue: 41%
- Non oil revenue: 28%
- Independent revenue: 16%
- Other revenues: 15%

Total: N5,080 billion

2018 Budget Proposal

- Oil revenue: 29%
- Non oil revenue: 37%
- Independent revenue: 13%
- Other revenues: 21%

Total: N6,606 billion

Note: Other revenues include tax amnesty, recoveries, signature bonus, JV equity restructuring, and grants & donor funding.

Source: Budget Office, PwC Analysis
### 2018 Budget Expenditure Proposals – Where the Money Going to?

#### 2017 Approved Budget

- **Statutory Transfers**: 6%
- **Debt Service**: 22%
- **Sinking Fund**: 31%
- **Non-debt Recurrent Expenditure**: 6%
- **Capital Expenditure**: 39%

N7,441 billion

#### 2018 Budget Proposal

- **Statutory Transfers**: 5%
- **Debt Service**: 23%
- **Sinking Fund**: 2%
- **Non-debt Recurrent Expenditure**: 2%
- **Capital Expenditure**: 40%

N8,612 billion

Source: Budget Office, PwC Analysis
Capital expenditure in the proposed 2017 budget

Allocating ~30.8% of the 2018 budget to capital expenditure at NGN2.428 trillion

Key sectoral capital allocations

- Power, Works and Housing: 23%
- Transportation: 11%
- Special Intervention programmes: 6%
- Defence: 6%
- Agriculture and Rural Development: 5%
- Others: 49%

Source: Budget Office, PwC Analysis
The oil sector remains the main source of export earnings and government revenues though its contribution to GDP has declined.

In 2017, Oil is estimated to account for:

- 96% of Nigerian export revenues
- 48% of Nigeria’s government income
- 10% of the Nigerian GDP

Source: NBS, PwC Analysis
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However, the low oil price has placed significant pressure on the currency and government earnings.

**Oil price vs. Exchange rate**

- **US$/bbl**
  - Brent Crude Oil Price (LHS)
  - Exchange rate (Interbank)

- **NGN/US$**

**Oil price vs. FX reserves**

- **US$/bbl**
- **Central Bank Liquid Reserve (RHS)**
- **BN US$**

Source: CBN, FMDQ, PwC Analysis

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Oil prices are not the only concern – production failures, spillages and high bunkering and theft rates affected volumes. However, volumes have increased recently due to lower incidence of attacks on facilities.

**Oil theft in Nigeria amounts to more than “$5Bn per year – an amount sufficient enough to fund universal access to electricity for all Nigerians by 2030” - IEA, 2014**

In 2016, oil production fell sharply due to militant attacks on oil and gas facilities. However, production has improved, rising from 1.5mbpd in August 2016 to 2.0mbpd in August 2017, as attacks moderated. Nonetheless, production fluctuation remains a major risk in the oil sector.

*Source: NNPC monthly bulletin, PwC Analysis*

*Nigeria's operating landscape • 2018 Budget*
Section 2 – Fiscal accounts

The tax base is much lower than other economies at a similar level of development. It is also poorly diversified; half of government revenue is dependent on oil

Government Revenue (2007-2016)

Source: FIRS, CBN, Nigerian Budget Office, Breakdown of Annual Oil Revenues (2012-2016)

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PwC
The government also has a limited ability to increase revenues through taxes on oil companies

Composition of Government’s oil revenue

Source: Nigerian Budget Office, Breakdown of Annual Oil Revenues (2012-2016)
Overall, only a limited portion of the oil revenues may filter through to support the real economy

Total Government revenues (2016)
(NGN4.9 trillion, shortfall of 36% from Budget expectation)

- Excess Crude Account
  - Oil: 9% (NGN242.7bn)

- Implicit Fuel subsidies
  - Oil: 0% (NGNo)

- 13% derivation of net oil revenue
  - Oil: 8% (NGN215bn)

- Joint Venture Cash Call & Oil Excess Revenue
  - Oil: 29% (NGN782bn)

- Local/state budgets
  - NGN86bn

- Federal Government of Nigeria Revenues (NGN3.0tn)
  - FGN share of revenues c.51% (NGN1.5tn)

- Other revenues (e.g. FGN independent revenues, 'augmentation of shortfalls')
  - NGN1.4tn

- Other financing:
  - Domestic debt issuance in 2016 (NGN0.3tn)
  - Special Accounts (NGN0.4tn)
  - Others (NGN1.5tn)

- Vat pool – revenues allocated to federal, state and local governments
  - Non oil: 32%

- Oil revenues (NGN2.7tn;55%)

- Non-oil revenues (NGN2.2tn;45%)

- Non oil: 32%

- Federal Government of Nigeria Revenues (NGN3.0tn)
  - Other revenues (e.g. FGN independent revenues, 'augmentation of shortfalls')
    - NGN1.4tn

- Other financing:
  - Domestic debt issuance in 2016 (NGN0.3tn)
  - Special Accounts (NGN0.4tn)
  - Others (NGN1.5tn)

- Capital expenditure (4%) c.NGNo.2tn
  - Others (14%) c.NGNo.7tn
  - Debt servicing (27.5%) c.NGNo.1.4tn
  - Statutory transfers (6%) c.NGNo.3tn
  - Recurrent expenditure (49%, of which 70% personnel costs) c.NGNo.2.5tn

Source: Budget office, PwC Analysis

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The biggest portion of federal government expenditure is the public sector payroll, accounting for 1.8% of overall GDP – equivalent to the total size of the livestock industry. There is limited scope to reduce government expenditure without cutting employment or wage levels.


Large levels of public expenditure have opened up a fiscal deficit over the last few years. The deficit is projected to remain elevated due to weak revenue accretion.
Despite this, outstanding government debt is low compared to countries within the region and those at similar levels of development.

Gross Public Debt (% GDP)

Source: IMF World Economic Outlook October 2017

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Of the NGN20.3trillion of outstanding public debt, the majority is denominated in domestic currency. However, the share of external debt is expected to increase, supported by the government’s refinancing plan.

### Outstanding public debt composition (NGN'Trn)

- **Domestic debt**: 80.0% in 2015, 82.4% in 2016, 82.4% in 2017E, 78.6% in 2018 FY
- **Foreign debt**: 16.8% in 2015, 20.0% in 2016, 17.6% in 2017E, 21.4% in 2018 FY

### Share of outstanding public debt

<table>
<thead>
<tr>
<th>Year</th>
<th>Domestic</th>
<th>Foreign</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>80.0%</td>
<td>16.8%</td>
</tr>
<tr>
<td>2016</td>
<td>82.4%</td>
<td>20.0%</td>
</tr>
<tr>
<td>2017E</td>
<td>82.4%</td>
<td>17.6%</td>
</tr>
<tr>
<td>2018 FY</td>
<td>78.6%</td>
<td>21.4%</td>
</tr>
</tbody>
</table>

Source: Debt Management Office, PwC Analysis


Nigeria’s economic recovery: Defining the evolution of economic growth

**Real GDP growth**

![Graph showing Real GDP growth from 2017 to 2022.]

### Sources: PwC Analysis

#### Scenario 1: Accelerated Policy reforms
- **Population growth rate**: 0.7%
- **Oil price (USD/bbl.)**: 60
- **Oil production**: 2.2%
- **Structural reforms**: Fast-paced implementation of structural reforms, particularly those related to the business environment

#### Scenario 2: Weak policy implementation
- **Population growth rate**: 2.0%
- **Oil price (USD/bbl.)**: 60
- **Oil production**: 2.2%
- **Structural reforms**: Sluggish implementation of structural reforms, with the drive for import substitution progressing at a slow pace

#### Scenario 3: Heightened political risk
- **Population growth rate**: 4.0%
- **Oil price (USD/bbl.)**: 60
- **Oil production**: 1.7%
- **Structural reforms**: Political tension accelerates in the wake of 2019 general elections, negatively impacting policy implementation

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Nigeria’s operating landscape • 2018 Budget
PwC • December 2017
## Lower oil prices, disruptions to crude oil production, and an unstable FX regime are the major near term risks

<table>
<thead>
<tr>
<th>Risks</th>
<th>Description</th>
<th>Potential impact</th>
<th>Likelihood of occurrence</th>
<th>Time horizon</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Lower oil prices</strong></td>
<td>• Failure of OPEC members to comply with production cuts agreement and increasing shale production</td>
<td>High</td>
<td>Low</td>
<td>Short to medium term</td>
</tr>
<tr>
<td><strong>Slowdown in key economies/Monetary policy normalization</strong></td>
<td>• Slowdown in economies with strong trade relations with Nigeria, particularly China, the UK, the US and India</td>
<td>Low</td>
<td>Medium</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td></td>
<td>• Ongoing monetary policy normalization in the US could lead to a reversal of foreign capital and restrict further flows</td>
<td></td>
<td></td>
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</tr>
<tr>
<td><strong>High inflation</strong></td>
<td>• Pre-election and 2018 budget spending</td>
<td>High</td>
<td>Medium</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td><strong>Oil production disruption</strong></td>
<td>• Attacks on oil and gas facilities by militant groups in the Niger Delta region</td>
<td>High</td>
<td>Medium</td>
<td>Short to Medium term</td>
</tr>
<tr>
<td><strong>Political risk</strong></td>
<td>• Pre-election uncertainties could elevate political tensions, and leadership succession could hamper policy continuity</td>
<td>Medium</td>
<td>Low</td>
<td>Medium term</td>
</tr>
<tr>
<td></td>
<td>• Referendum in the South-East region</td>
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<tr>
<td></td>
<td>• Continuous insurgency in the Northern region</td>
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</tr>
<tr>
<td><strong>Deterioration in the Banking sector</strong></td>
<td>• Worsening financial soundness indicators such as high Non-performing loans and low capital adequacy</td>
<td>High</td>
<td>Low</td>
<td>Short term</td>
</tr>
</tbody>
</table>

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