The Lagos Chamber of Commerce & Industry

Economic and Business Review in 2017 and Outlook for 2018

2017 ECONOMIC REVIEW

The economic and business performance in 2017 was mixed. The economic downturn of 2016 continued into the early part of 2017. However, there was an upturn with the resumption of growth in the second quarter of 2017. Though the growth was very marginal at 0.55%, it marked a significant turn of events. The economic outlook since then had remained positive, though the recovery and growth have been fragile. The non-oil sector recovery was somewhat slow because of issues of operating cost, investment climate and productivity faced by economic players. Indeed, the non-oil sector contracted by 0.8% in the third quarter of this year. However, the trajectory for growth and investors' confidence remains positive for 2018.

Exit from Economic Recession

The Nigerian economy plunged into recession in August 2016, when the Gross Domestic Product (GDP), contracted for the third consecutive quarter. However, after five consecutive quarters of contractions, the economy exited from recession with a marginal growth of 0.55% in the second quarter of 2017, and 1.4% in the third quarter.

This presented a positive outlook for Nigeria's economic outlook and boosted investors' confidence. The major drivers of the recovery were:

- Improvement in crude oil price and oil output
- Improvement in liquidity in the forex market
- Commitment of Government to ease of doing business

While appreciating the exit from recession, what is paramount is the impact on the cost of doing business, productivity of the investors, competitiveness of firms and the sustainability of investments. And to the average Nigerian, what matters is the effect on welfare, especially lower food prices, reduced cost of healthcare, improved transportation system, constant power supply and security of lives and property. With unemployment rate at an all-time high of 18.8% in the third quarter of 2017, and many employers including the public sector finding it difficult to pay workers as and when due in 2017, we need to worry about recovery and rapid job creating growth as we move into 2018.

Foreign Exchange Market

CBN's periodic intervention in the Forex market reduced the exchange rate volatility over the last two quarters of 2017. With the intervention, businesses witnessed improved liquidity of forex and stability of Naira against the dollar. Confidence is gradually returning to the forex market and we hope that this would be sustained in 2018. However, economic players stated that it was impossible to access the foreign exchange at the official rate of N305 to the dollar.

Crude oil prices in the international market and local production levels of crude oil remain the two key variables that would determine the sustainability of the current favorable FOREX regime.

The multiplicity of exchange rates remains a concern because of the implication for transparency and round-tripping in the FOREX market. It is thus desirable to reduce the multiplicity of rates and the disparities in the rates to further deepen confidence in the market.

Inflation

Headline inflation rate trended down from 18.72 in January to 15.91 in October 2017. Core inflation remain relatively lower at 10.2% compared to food inflation which ended at 20%. It is noted that while the impact of foreign exchange fluctuation on prices may have moderated, food supply and its linkages such as transport and logistics remain a big issue in the country. This is partly the consequence of the decline in farming activities due to the security challenges of farming caused by the continued insurgency in the North East and activities of hersmen across the country.

Interest Rate

Access to and cost of fund (interest rate) remain big issues for domestic investors in 2017. With commercial bank lending rate at 22-35% depending on the borrower and other factors, it is difficult to sustain a business enterprise under such credit condition. We note the efforts of government through CBN and Bank of Industry (BOI) to extend intervention funds to operators at lower cost. However, the range of beneficiaries and economic wide impact remain very low.

Also, the President in 2017 signed into law two bills that seek to improve access to credit for MSMEs in Nigerian. The 'Acts' are the Secured Transactions in Movable Assets Act, 2017 (otherwise known as Collateral Registry Act) and the Credit Reporting Act, 2017. We hope that the laws are enforced to help unlock credit to investors in the economy in 2018.

Foreign Reserve

Foreign reserve recovered significantly from a low of $23 billion in October 2016 to $38.2 billion in December 2017. This is a major source of confidence for investors and other stakeholders on the capacity of the economy to defend the local currency and meet foreign financial obligations. We expect the foreign reserve figure to pass $40 billion mark in 2018 if this trend continues.

Capital Market

The Nigerian Stock Exchange (NSE) posted impressive performance in 2017. For instance, year to date, the index returned about 40% and market capitalization reached a peak of N13.2 trillion. This performance is largely the outcome of recovery in key macroeconomic indicators and a boost to investor confidence during the year. For instance, equities became the preferred asset class for portfolio investors in Q3-2017. According to the National Bureau of Statistics (NBS) Q3-2017 report, $4.1 billion was imported into the country out of which $2.1 billion was portfolio investments.

The trend was driven by improved macro-economic outlook and the enhanced investor sentiments. These were driven by the policy reforms such as the creation of the Investors and Exporters window and increased dollar liquidity. Also, the headline inflation maintained a downward trend. The improved economic performance also played a significant role.

It is expected that economic growth will be stronger in 2018 and this is expected to impact positively on the stock market. However, the impending general elections, mean that some foreign portfolio investors may unwind their positions on the NSE in late 2018 and return after the elections. This could lead to a drop in share prices and slowdown in the performance of capital market.

Ease of doing Business

Nigeria moved 24 places in the World Bank Ease if Doing Business ranking from 169 in 2016 to 145 in 2017. The report covers190 countries and focuses on the ease of doing business reforms effected by government to improve business activities.

Nigeria Ranking on the World Bank Ease of Doing Business

Topics	DB 2017 Rank	DB 2016 Rank	Change in Rank
Ease of Doing Business	**145**	**169**	**+24**
Starting a Business	138	139	+1
Dealing with Construction Permits	174	175	+1
Getting Electricity	180	182	+2
Registering Property	182	181	-1
Getting Credit	44	59	+15
Protecting Minority Investors	32	20	-12
Paying Taxes	182	181	-1
*Trading Across Boarders (Ports)	181	182	+1
Enforcing Contracts	139	143	+4
Resolving Insolvency	140	143	+3
Distance to Frontier (%)	44.63	44.69	+0.06

Source: World Bank Ease of Doing Business Report – 2017

We applaud the reform initiatives of the Federal Government driven by the Presidential Enabling Business Environment Council (PEBEC). The series of

Executive Orders issued by Federal Government in 2017 and targeted at promoting the ease of doing business seem to be yielding the desired improvement.

However, the methodology for the computation and ranking of countries needs to be reviewed to include some country-specific variables of the Nigeria business environment such as state of security, quality of institutions, infrastructures and credits. These limiting factors are not covered in the metrics used by World Bank in its ranking. Another downside is that the World Bank survey covers only two cities, Lagos and Kano as a proxy for the entire country.

Ports Situation

In 2017 users and operators at the Nigerian Ports faced some major challenges and bottlenecks namely, deplorable state of roads leading to the Lagos Ports - Apapa and Tincan Island Ports, infrastructure and technology breakdown; while we acknowledge the ongoing collaboration between some private firms and Government to fix the port roads there is need for urgent palliative measures to enhance movement of traffic in this axis.

Poor access to the ports due to bad state of the roads and absence of functioning rail had multifarious effects on the private sector, economy and the citizens. Some of these effects are as follows:

- Risk to the lives of citizens arising from Containers falling off the trucks as a result of bad roads. Several lives have been lost in recent past as a result of this.
- Congestion at the Ports resulting from the delay in the evacuation of cargo from the Ports.

- High demurrage paid by importers to Terminal Operators and Shipping Companies as a result of delay in the clearance and evacuation of cargo in the Ports.
- High cost of transportation for evacuating cargo because of the prolonged engagement of the trucks by importers arising from the delays.
- Traffic congestion along the roads leading to the Ports, which often spills over into the Lagos Metropolis causing severe traffic jam and loss of man hours in Lagos.
- Delays in getting raw materials and other inputs from the Ports to the factory premises in Lagos and other parts of the Country.

Estimates from LCCI research on "Maritime Ports Reform" show that hundreds of billion of naira are lost annually due to inefficiencies and inherent shortcomings in the nation's ports. To achieve the much-needed efficiency and productivity in the Nigerian Maritime Ports the following reforms and policy measures are essential:

- Adopt and enforce an Integrated Advance Cargo and customs clearance system, with scanning, and tracking (SST) capabilities.

- Implement the National Trade Data Centre project that is readily accessible to all agencies, operators and stakeholders at all times and everywhere to eliminate inherent abuses

- Full Implementation of a Single Window Platform. This is the most vital reform measure with potential to create immediate cross-cutting positive impact in the port.

- Expand Private Sector Investment, building and management of ports infrastructure such as roads, rail and truck parks with online call-up systems.

- Enforce the Presidential Order that reduced the number of public sector Agencies/Departments from 14 to 6 at the ports

- Shipping companies to establish adequate holding bay for empty containers.

- Use of pipelines for the evacuation of petroleum products from the Lagos ports would considerably ease congestion on the Apapa corridor.

In line with the findings of LCCI research, it is believed that the port can double its 2016 non-oil volume of 1.1 million TEUs over the period, 2018-2019 if the above reform measures are implemented. This has a potential of creating new 10,000 jobs within the port sector and lead to approximately 800,000 additional jobs in the industry over the same period.

Power Situation

The provision of power remains at the heart of ease of doing business in Nigeria. We note and commend the efforts of the Government in addressing the perennial power supply shortage and deeper commitment to sources of power and off-grid initiatives.

However, the power situation continues to pose severe challenges to business operators. There were concerns across sectors about high energy costs especially high expenditure on diesel, cost and availability of gas. These continue to impact on the bottom line of investors especially those in the real sector. SMEs and some processing companies reported that they spend as much as 20-25%% of their total operating cost on provision of alternative power supply and payment to DISCOs.

SECTORAL REVIEWS

Sectoral performance in 2017 as follows:

Agricultural Sector

The sector benefitted from the inward-looking disposition which the recession created in the economy. In particular, the weak naira made imports more expensive and local products more competitive.

However, the sector grappled with a number of challenges which constrained its growth in 2017. These include the following;

- Acute scarcity of parent stock for Turkey which severely constrained the capacity of poultry owners to expand the production of live turkey.
- Cost of vaccines and micro nutrients for the production of fishmeal and other livestock feeds was very exorbitant. This contributed to the high cost of poultry products. The situation was further compounded by the Nigeria Customs Service that classified micro nutrients for the production of poultry feed as finished goods, rather than raw materials.
- Investors in the sector could not access foreign exchange at the official rate of N305 to the dollar.
- Multiple government agencies still pose problems for importers of agricultural inputs at Lagos ports.

- Farm machinery and equipment as well as agro-chemicals were not accessible by many farmers during the year. The costs were prohibitive, and the expected support from the government (State & Federal) was not forthcoming.
- Interest rate on loans for agricultural purposes was also prohibitive at between 25-30%

Real Estate

The following factors impacted the performance of the real estate sector in 2017.

- There was a drop in effective demand, following the general economic downturn triggered by the economic recession. The sector is yet to recover from the setback and the depressed demand that came with the recession.
- Property vacancies was high during the year especially at the high-end segments of the real estate market. This was attributed to reduction in the number of expatriate staff in many organisations. Secondly, it was also a reflection of the downturn in the economy which affected the demand for high end properties.
- Because of the depressed demand, property prices are gradually declining.
- Funding remains a big challenge for the sector. The cost of fund was as much of a problem as the tenure of funds. The economy has no long-term fund to support the sector. There is practically no mortgage finance system in the economy.
- Default rate or rent also remained high during the year.

Non-Oil Export Sector

The non-oil export sector was impacted positively by the depreciation in the Naira exchange rate. This led to improved performance of the non-oil export sector even in the face of recession and the fragile economic recovery. However, investors in the export sector expressed the following concerns;

- The export stimulation fund promised by the CBN is yet to be made available to exporters. It is believed that the release of this fund will have a major impact on the export sector. The fund is N550billion.
- Production cost by exporters remains high, largely because of infrastructure issues. This is affected the competitiveness and the profit margin of exporters.
- Facilities for testing of the quality of the export products and the generation of quality reports are still lacking in the country. Reliable testing facilities are necessary for the generation of credible quality assessment report. The solid mineral sector is the most affected by this challenge. It is therefore very important that government puts in place standard quality testing laboratories for exporters and for export products in 2018.
- Access roads to Lagos ports was a nightmare for exporters in 2017. The delays posed significant risks to the quality of export products, especially agricultural export products.
- The cost of transportation of export products from the hinterlands to the cities has become astronomical. This is also a major factor affecting the competitiveness of export products. This is particularly the case for export products that have a lot of weight.
- The incursion of foreigners into the export of primary products and the consequent crowding out of domestic exporters was a major concern for the exporting community in 2017. One example is that of the export of processed food.
- Exporters expressed concern over the introduction of exorbitant handling charges by Terminal Operators at the Lagos port. N40,000 was imposed on 20foot container and N60, 000 on 40-foot container for export.

Manufacturing Sector

The situation with the manufacturing sector in 2017 was that of a partial relief, especially with respect to access to foreign exchange. Manufacturers reported an improvement in the liquidity of the foreign exchange market. These enhanced their capacity to import raw materials and boosted capacity utilization. However, manufacturers expressed concern with respect to the following;

- High interest rate is between 25-30%. This has resulted in high operating cost for manufacturers.
- Dearth of long term funds.
- Infrastructure situation with respect to power and energy and logistics, especially the impact of the bad roads on the cost of transportation.
- Inflow of fake and sub-standard products remains a major challenge for manufacturers in 2017.
- Weak patronage of locally produced goods, especially by government agencies and ministries.
- Some manufacturers lamented the adverse effect of the activities of the Federal Operations Unit (F.O.U) of the Nigeria Customs Service on their businesses. There were recurring instances of arbitrary arrests, impounding of containers duly cleared at the ports and extortion by operatives of the FOU

- Concerns, were also expressed about indiscriminate valuation queries by the Nigeria Customs Service. These are clearly not in consonance with the vision of ease of doing business currently being pursued by the government.

Automobile Sector

- Many operators in the sector lamented the high cost of vehicles which depressed sales, and profitability. Sales of new vehicles dropped from over 80,000 units per annum few years ago to less than 20, 000 units currently.
- Most operators expressed concern over the Automotive Policy which contributed to the high cost of automobiles in the country. They called for an urgent review of the policy and reduction in import duty on vehicles. This has become even more imperative because of the over 100% depreciation in the naira exchange rate over the last two years.
- There is need for more support and incentives to motor vehicle assemblers to reduce their production cost.

OUTLOOK FOR 2018

The fundamentals of the economy are improving with numerous opportunities and potentials. Crude oil prices and output levels have recovered, foreign reserve is improving, and inflation is on a steady decline. It is expected that these impressive outcomes will be sustained into a better part of 2018.

Given the prevailing economic fundamentals and with government commitment to sustain economic reforms, we project the following:

- GDP growth to record 3-4% in 2018;
- Oil price to average around $50 per barrel;
- External Reserve to hit $40 billion mark; and
- Headline Inflation at 13%.

For the country to sustain the present of recovery and achieve the growth forecast, we suggest the following enablers:

- Aggressive investment in infrastructure to boost productivity in the economy.
- Reduction in multiplicity of exchange rates
- Alignment of procurement policies at all levels of Government to support domestic investment
- Investment policy that would protect domestic investors
- Tax policy that is investment friendly
- Interest rate policy that is investment friendly.

Current reforms in such critical sectors as power, agriculture, solid minerals and oil and gas should be sustained. The executive orders signed in May this year should be fully enforced to improve the way Government does business and thereby improve the business environment.

LAGOS CHAMBER OF COMMERCE AND INDUSTRY

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