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Key Investment Themes for 2024.

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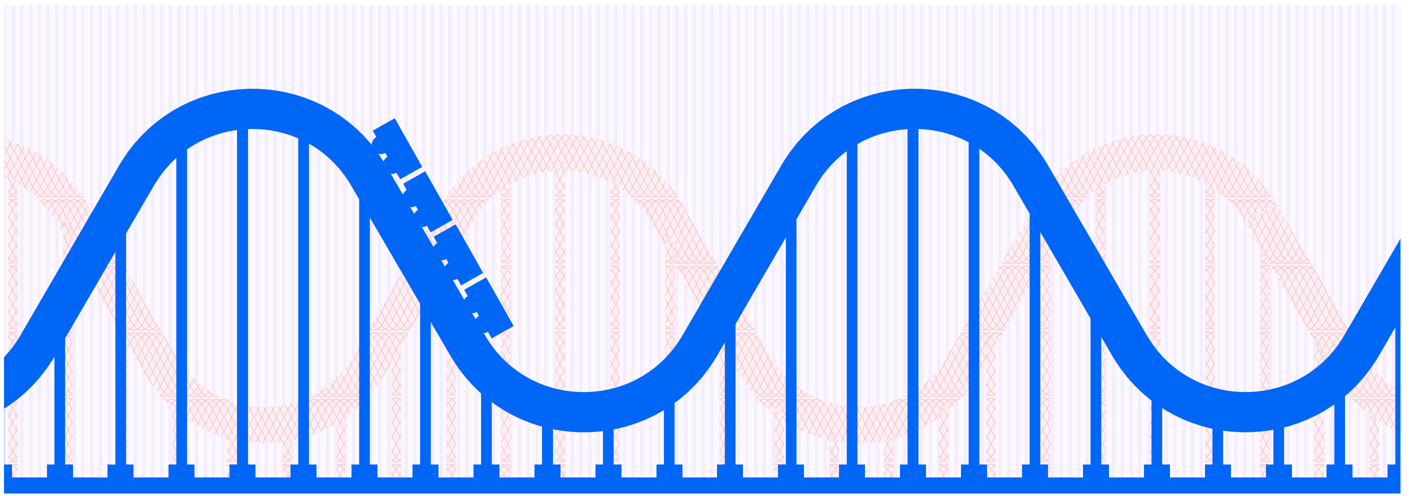
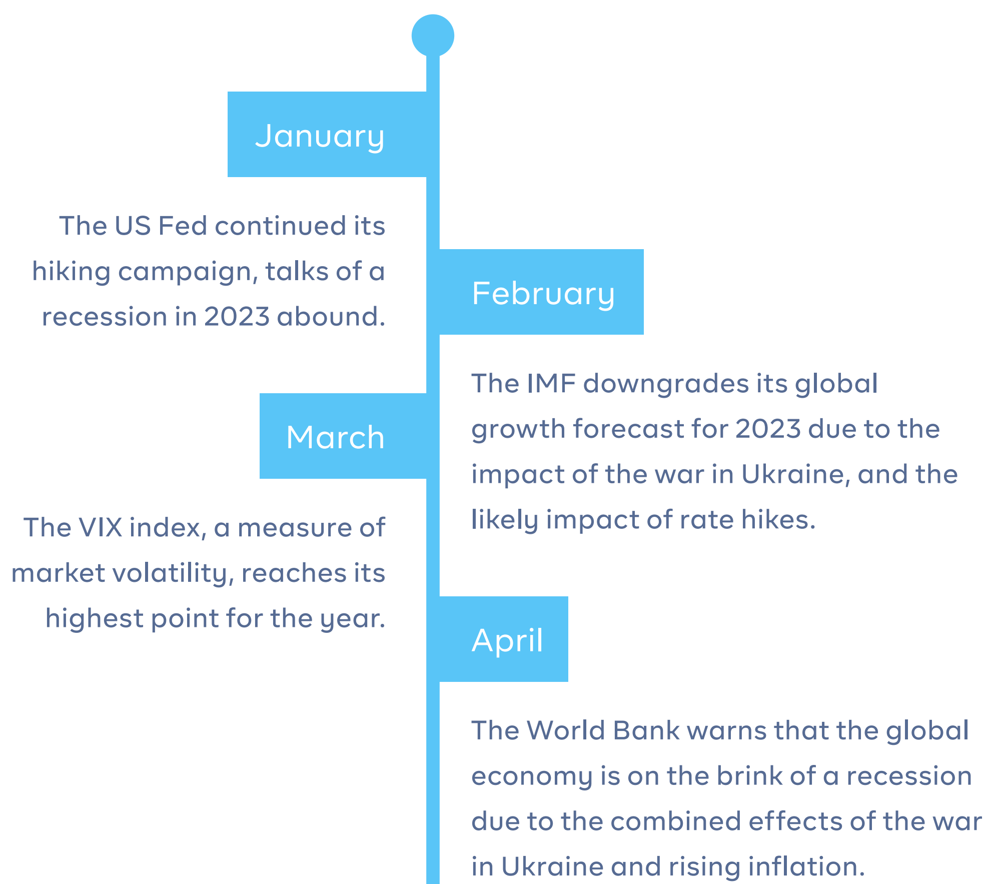
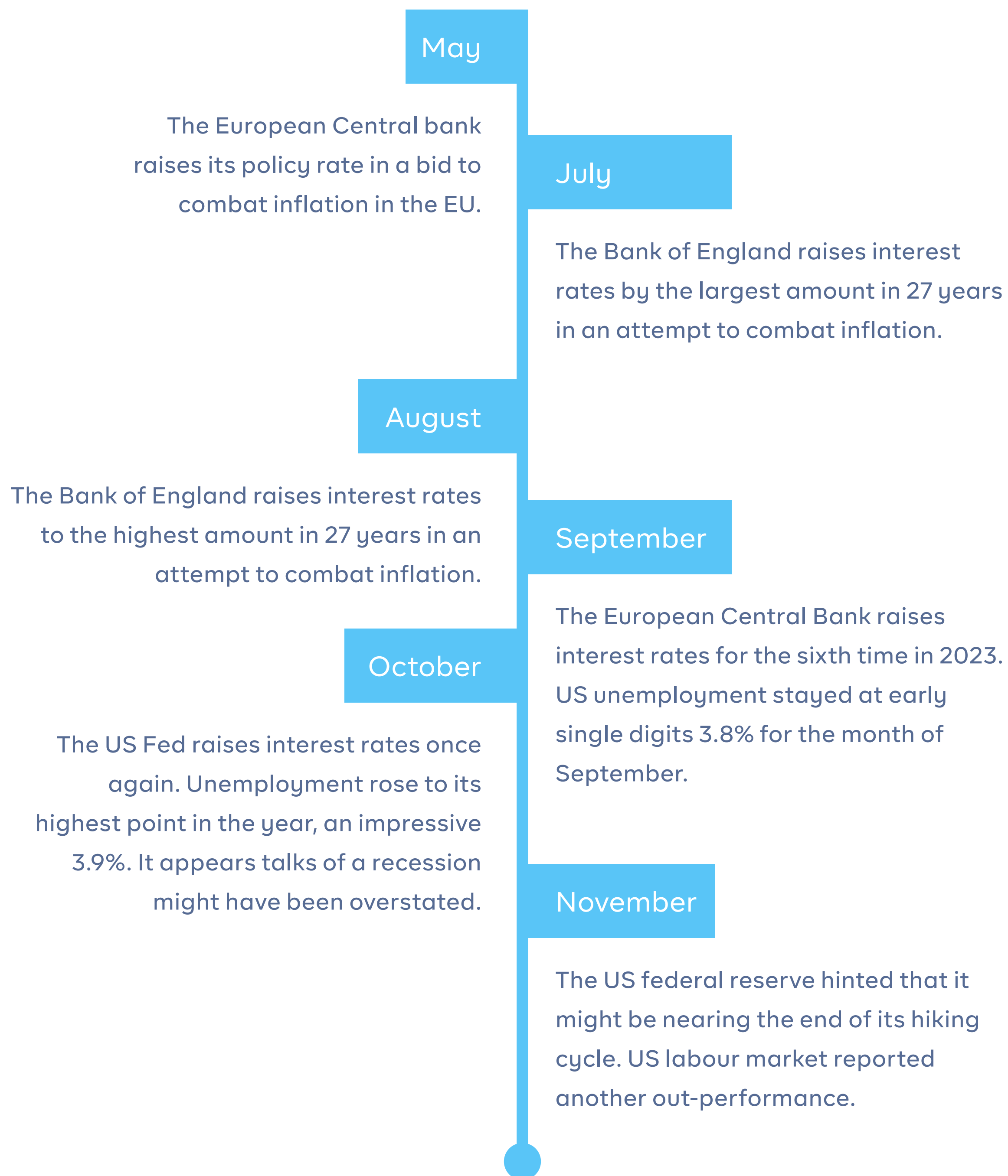


The year 2023 was a roller coaster year for investors due to the continuous contrast between macroeconomics and Geopolitics. Notably, a robust and resilient American economy, shaped by a heightened emphasis on adaptability in the aftermath of the pandemic among other factors, successfully moderated the impacts of the Russo-Ukrainian war and the global central banks' efforts to combat inflation on financial markets.

Fig. 1: Timeline of key global economic events in 2023





In Nigeria, the 2023 election ushered in a new set of administrators for the country which was followed by a host of policy reforms like the removal of fuel subsidies as well as a devaluation of the currency to a more market-reflective rate. Though these policies are beneficial to the country's long-term economy, the immediate impact was a surge in the price of food and energy with inflation reaching a 18-year high of 28.2% in December 2023. This surge in inflation meant that the purchasing power of Nigerians was reduced as many citizens could now only afford fewer goods and services with some citizens even reportedly cutting back in some essential items. In 2024, we believe an understanding of the key themes both in the global economy and

in Nigeria, would be crucial to having a successful investment journey. In this piece, we spotlight the key investment themes likely to dictate the pace of capital markets in 2024.

Theme 1 – FX: The worse is likely over.

The topsy-turvy nature of the country's currency has turned all 200 million of its citizens into FX traders, as they are constantly monitoring the exchange rate to ascertain whether their FX position (Read purchasing power) is still tangible. In 2023, the Local currency began the year at the official window at an exchange rate of N461/$ and as at the timing of this report, it stood at N865/$. At the parallel market, the exchange rate hasn't fared any better, falling by 67.5% to N1243/$ as at the timing of this report.

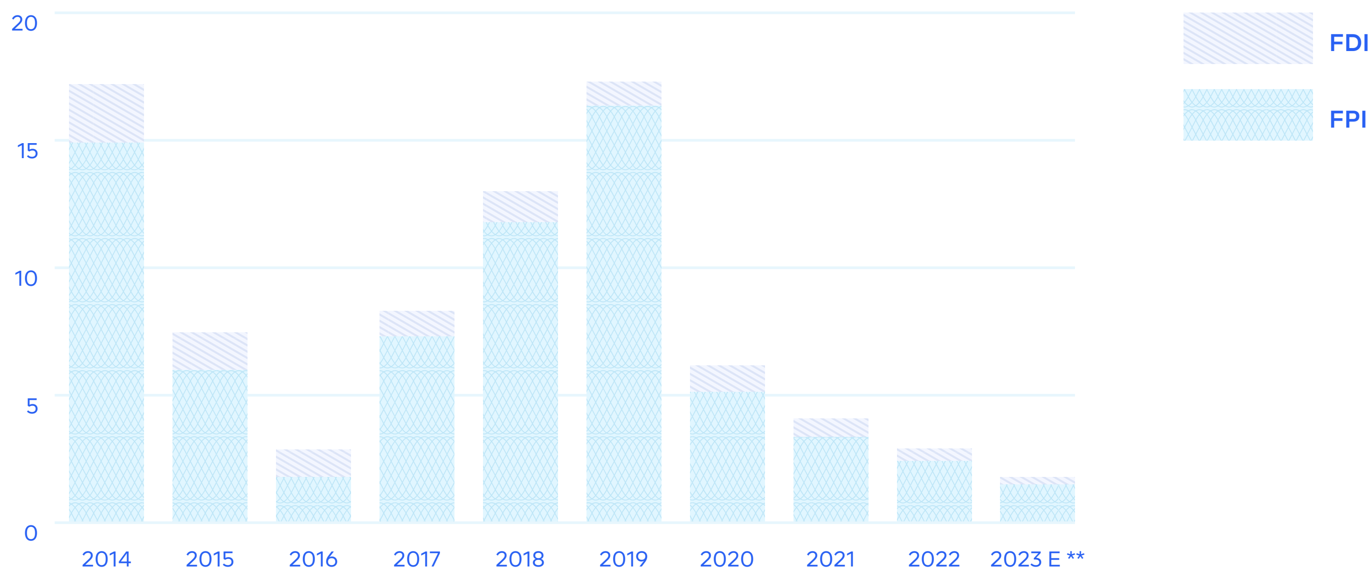
Fig. 2: Chart on YTD FX rates at both windows.

This persistent decline in the exchange rate across the years is mainly due to two main reasons.

1. Weaker FPI and FDI inflows. The CBN's financing of the Federal government despite its contractionary policy stance ensured that yields on government instruments were artificially low and with inflation rising unabated real interest rates in Nigeria went below zero. The Impact of this was that FPI's with their $ decided investing in Nigeria wasn't worth the risk leading in no small part to the severe dollar illiquidity we are currently facing. Meanwhile, capital controls from the CBN to arrest the capital flight

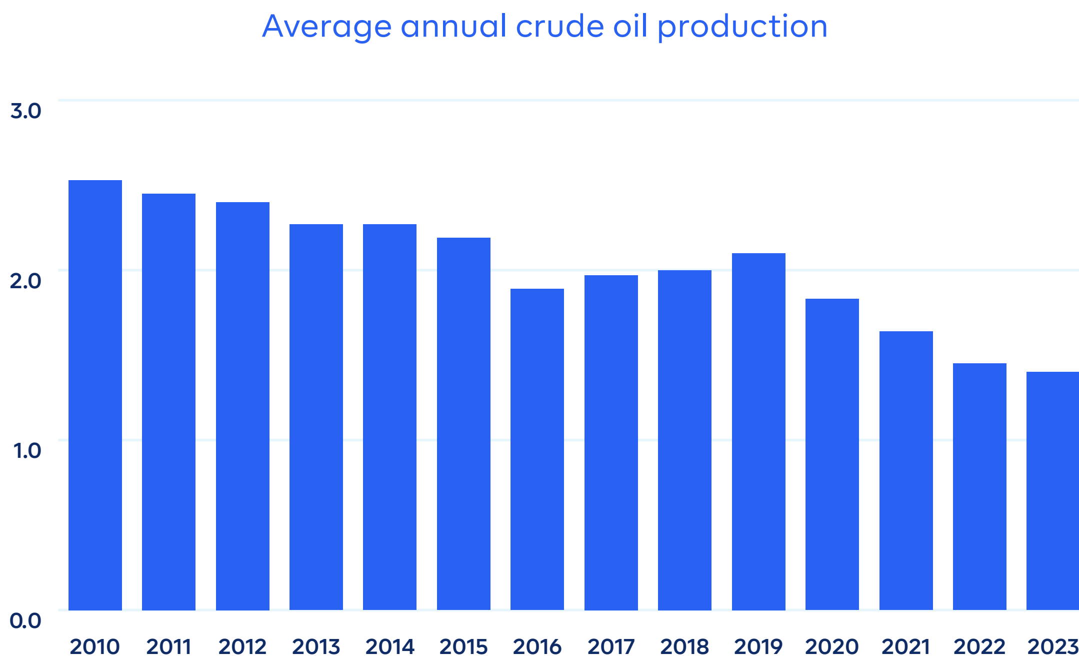
didn't exactly help and only led to multiple exchange rate systems, FX repatriation issues. With no new dollar coming in from foreign investors and the investors in Nigeria anxious to leave the pressure on the currency continued to build up.

Fig. 3: Chart of FPI inflows and real interest rates in Nigeria.



2. Grand theft auto in the Oil & Gas sector. The Oil industry in Nigeria has remained the golden geese, helping the CBN to meet its $ obligations as it accounted for a large chunk of the country's foreign exchange earnings (82.5% of exports in Q3'23). Persisting cases of oil theft have however meant that the $ taps are currently being hampered and as a result the CBN has been unable to meet its dollar obligations as at when due.

Fig. 4: Chart on oil production and FX reserves in Nigeria.



The new administration has however made moves to address both issues. On the first point, the new CBN governor Mr Yemi Cardoso announced a return to a more orthodox monetary policy regime and has made moves to strengthen the monetary policy transmission mechanism. In English, this means that the interest rate on government securities is expected to increase. Already, yields on short-term and long-term naira assets are currently higher than the pre-Cardoso era and although real interest rates are still below zero, we believe this is a step in the right direction.

The fiscal authorities have also indicated a strong drive to curb oil theft and increase oil production. The Nigerian National Petroleum Company (NNPC) for example recently announced that Nigeria's oil production could hit 2.2 million barrels per day in 2024. This increased oil production if achieved could support the country's FX position in the mid to long term.

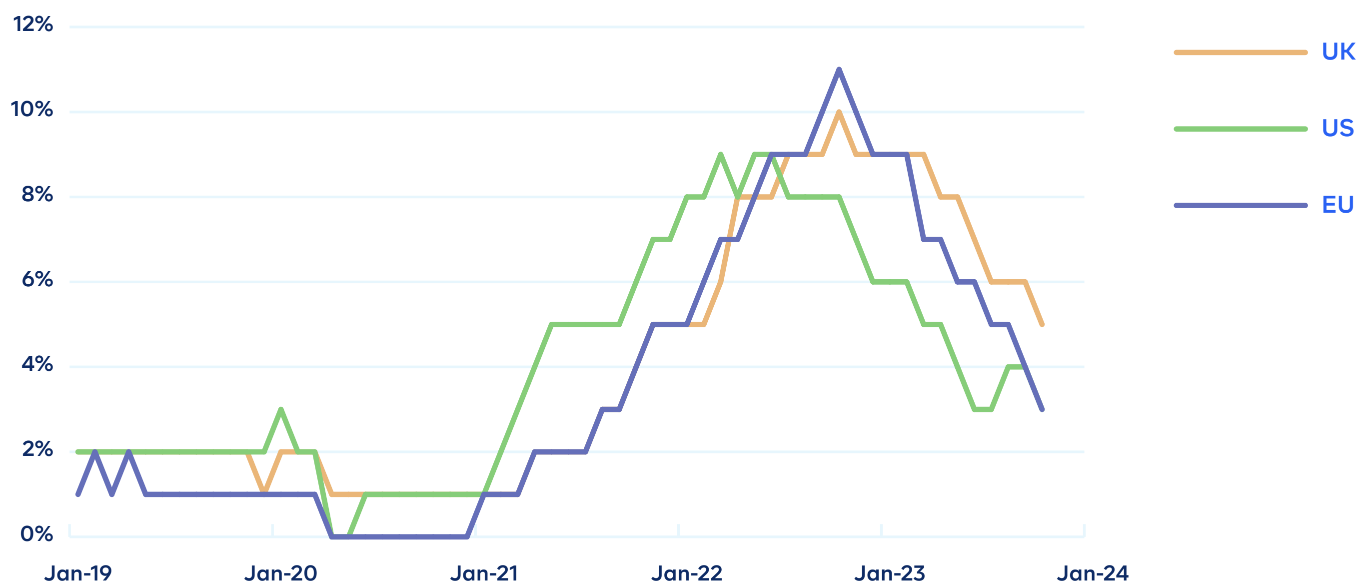
Theme 2 – Inflation: All roads point southwards.

- **Global; Inflation peaked in 2023.**

In 2023, global investors were mainly concerned about inflation. This was triggered by a combination of a war-driven energy crisis and an oversupply of money from years of expansion policies in developed countries. As a result, the Consumer Price Index

(CPI) in many major economies hit multi-year highs. However, as the year progressed the impact of a generally tighter monetary policy stance combined with base effects from the previous year, brought inflation to controllable levels. For example, inflation in the US collapsed from a peak of 9% to under 3.5% currently and is on track for a third consecutive monthly decline In December.

Fig. 5: Inflation seems to be on the downturn.

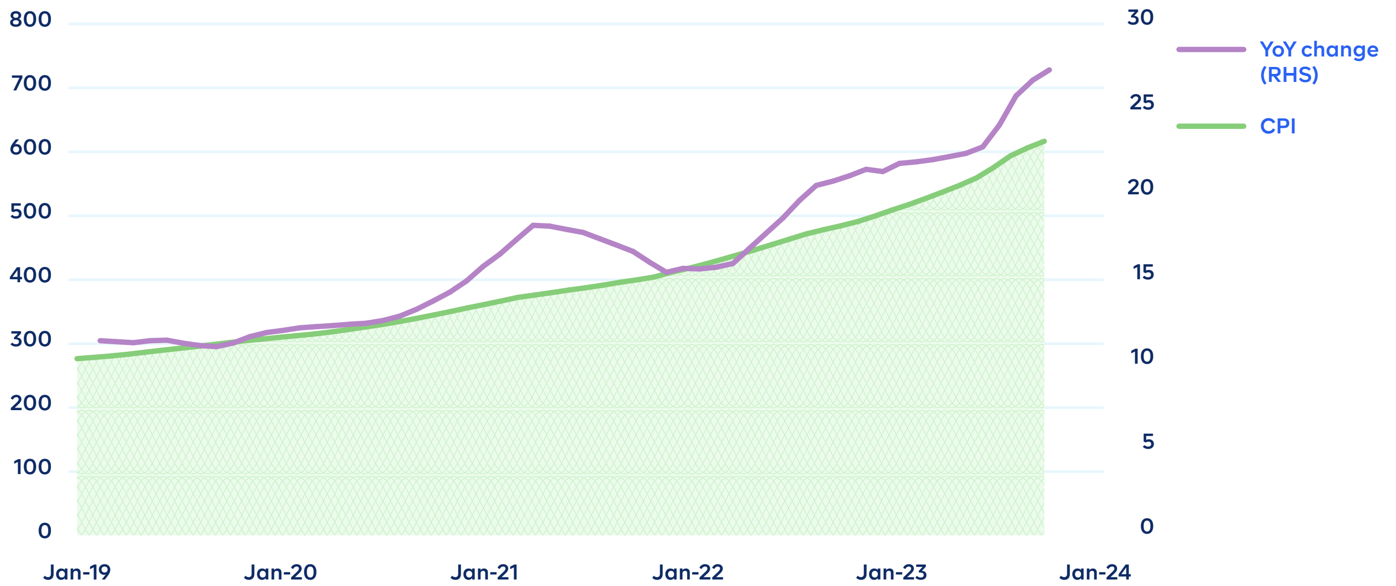


Though inflation remains a significant concern for individuals, businesses, and policymakers worldwide, we are more optimistic going into 2024. This is because the fight against inflation by central banks which is already yielding fruits looks set to continue into the new year. This could mean that barring any unforeseen circumstance a likely return to multi-year highs in the new year is unlikely.

Locally: Policy rejig might support decline in H2.

Inflation in Nigeria has been on an upward trajectory since 2019 due to security-related disruptions in food production and distribution in Nigeria's food-producing regions and a depreciation of the Naira - which in turn is making imported goods more expensive. This situation was further compounded in 2023 with the removal of the subsidy in May and a unification to a more market-reflective exchange rate in June. Going into the new year, inflation is likely to continue to be a drag on consumer wallets in Nigeria particularly in the first half of the year. We however see legroom for improvement in H2'23 due to 1) the lagged impact of the recently commenced tighter monetary policy framework of the CBN. 2) the impact of a higher base from H2'23.

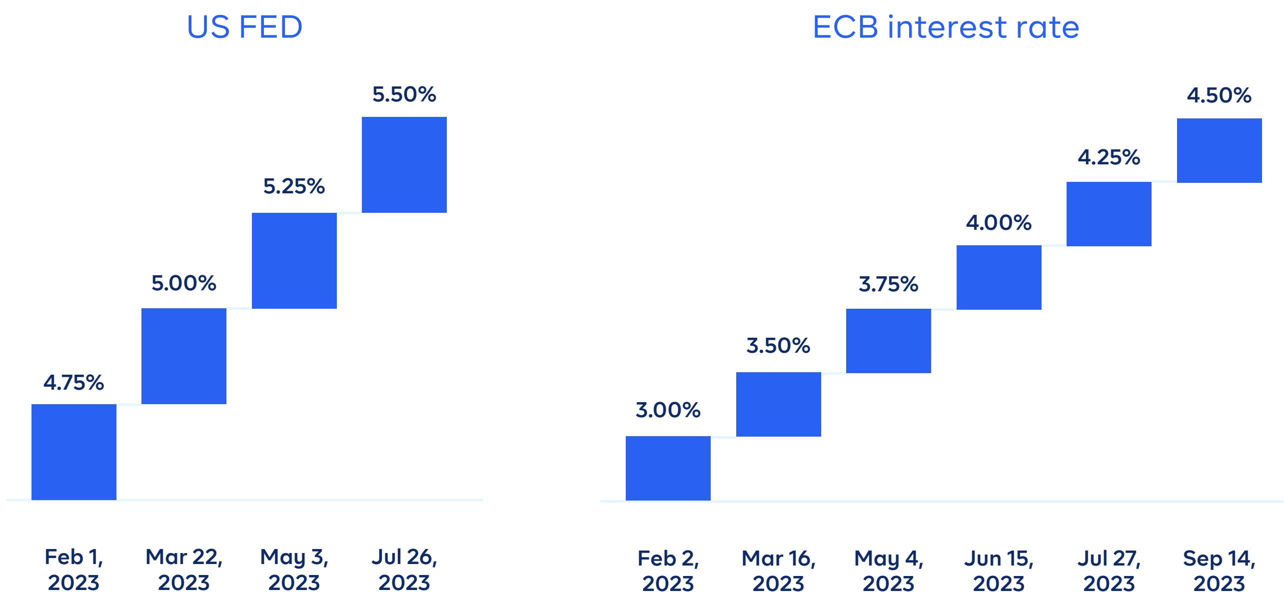
Fig. 6: Chart on inflation in Nigeria since 2019.



Theme 3- Central Banks and monetary policy: Prepare for a dovish year.

As earlier mentioned, global central banks successfully waged a war against inflation in 2023 as they shifted to a tighter monetary policy stance. The US FED for example raised its monetary policy rates a total of four times in 2023, taking its federal funds rate range from 4.25% to 4.50% in January to 5.25% to 5.50% as of the time of writing this report. The ECB in its own bid to fight inflation, raised its policy rate a total of 6 times in 2023.

Fig. 7: Chart on US and ECB rate hikes.



With the inflation in major developed economies on the decline, central banks are unlikely to sustain the same level of tightness in their monetary policy in the new year, however, we expect central bankers to adopt a wait-and-see approach in early 2024 as they try to avoid a premature loosening which could reignite inflation. We expect the US FED to stand pat on its monetary rate for the most part of H1'24. In the second half of the year, we could however see a reduction in monetary policy rates if the prognosis of lower inflation turns out to be true.

Emerging markets could benefit from flat to falling interest rates.

Emerging market economies Like Nigeria most of which recently commenced their hiking campaign could potentially benefit from a relatively dovish stance in developed markets as higher interest rates in developing economies can make emerging markets more attractive to foreign investors leading to an increase in capital inflows, boosting economic growth and development.

Theme 4 – E is for Energy: We might see some improvement.

The price of crude oil is arguably one of the single most important economic variables in Nigeria as it has a direct impact on various sectors like government revenue, foreign exchange availability and liquidity the price of manufactured goods and services (Diesel is a common source of energy for manufacturers in Nigeria) because oil accounts for a large chunk of government revenues and foreign exchange earnings.

The implication of this reliance is that when crude oil price is high, the government generates significantly more income from oil exports. This can boost fiscal spending on infrastructure, education, healthcare, and other critical areas. Higher oil revenues can also lead to a stronger naira as earlier mentioned, making imports cheaper and potentially boosting consumer spending and businesses' competitiveness. However, the deregulation of the downstream oil sector could mean the price of Automotive Gas Oil (Diesel) and Premium Motor Spirits (Petrol) is likely to go up and put some pressure on consumer wallets. When oil prices fall, the government also generates less revenue for its use, and the currency runs the risk of devaluation though there is a likelihood of cheaper AGO and PMS.

Indicators suggest weaker crude oil prices in 2024.

Across the globe, oil demand growth appears to be decelerating due to 1) Tighter financial conditions and 2) Economic weakness in the world's largest energy importer (Spelt China) There is also the ever-lingering risk of an economic downturn in the US in the upcoming year. Already, economic forecasters like the U.S. Energy Information Administration (EIA), Goldman Sachs and the World Bank have announced reductions in their oil price forecast for the new year. The implication of this could be a reduction in government revenue though the forecasted increase in oil production could provide a respite. On the flip side, AGO and PMS prices might improve in the coming year.

Geopolitics: Russo-Ukraine and Gaza pose downside risks.

In the modern interconnected global village, in which we all live, the influence of global geopolitics on investment has become more important as events in seemingly obscure corners of the globe increasingly continue to shape the economic landscape. The Russian invasion of Ukraine for example had ripple effects on global investment as it sent shock waves across global supply chains which in turn led to an energy crisis and spiraling inflation the world over. Going into 2024, there are four key geopolitical themes worth keeping an eye on.

Russia vs. Ukraine.

The war in Ukraine is still ongoing after two years with no clear end in sight, with both sides continuing to suffer heavy losses. Diplomatic efforts have largely stalled, with no viable peace agreement in sight. Going into the new year, the war's economic impact could potentially intensify and lead to further supply chain disruptions and energy price volatility. It could also lead to increased risk aversion as the uncertainty and instability could lead investors to become more risk-averse, decreasing investments in emerging markets like Nigeria.

Isreal vs Gaza.

Despite recent ceasefires, the underlying tensions between Israel and Hamas, the Palestinian militant group controlling Gaza, haven't disappeared. Flare-ups and violence continue sporadically, while negotiations for a lasting peace agreement have

been stalled, leaving no clear path forward. Though the conflict is in its early phase, it has the potential of spilling over and destabilizing peace in the entire region. This could affect countries like Lebanon, Syria, Jordan, Egypt, Saudi Arabia, and Iraq with dire consequences for oil production.

Finding Calm in Turbulence: 2024 Asset allocation Guide.

2024 looks set to be filled with both economic and geopolitical uncertainties for investors and as always, we believe the key to a successful investment strategy this year is to ensure a well-diversified portfolio to enable you well weather the storm that lies ahead. For our 2024 asset allocation, we increase our allocation to money market funds (35% vs 30% last year) considering their improved yields and the liquidity profile which could come in handy during periods of high volatility. We retain bond funds at 20%, which is important for regular income generation. Though we advise a focus on short-duration papers due to the possibility of higher yields in 2024 for FGN securities We also increase our allocation to equity mutual funds (25% vs 20% last year) our increased optimism for stocks is based on the impact of tamer inflation on consumer wallets which could bode well for corporate earnings. We retain our 20% allocation to dollar mutual funds and 10% allocation to cash.

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