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Economic Research

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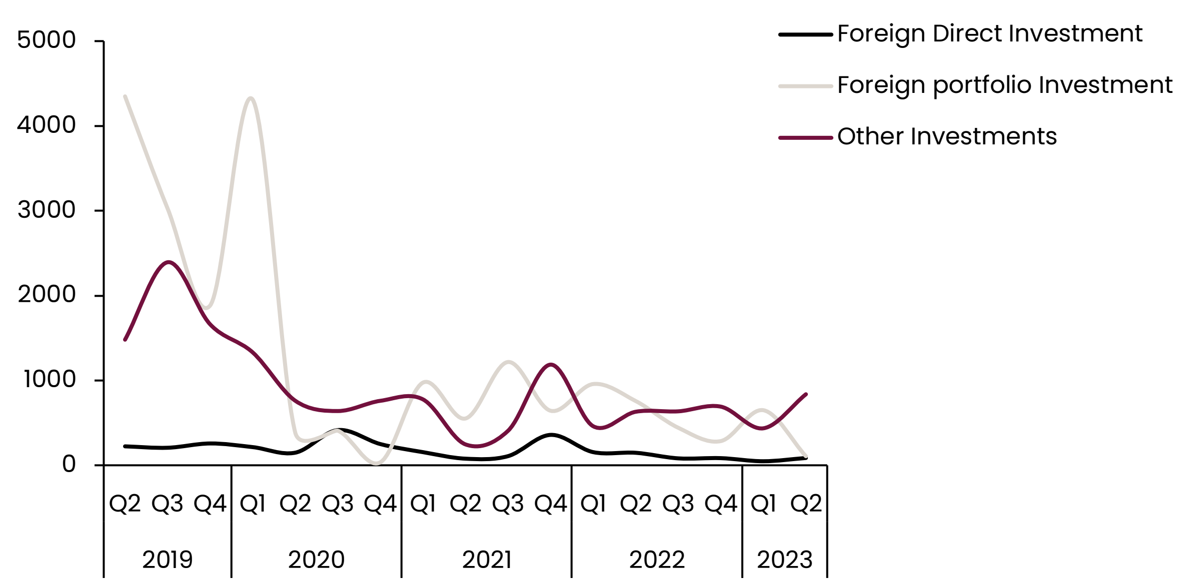
Q2:2023 Capital Importation

Structural Issues Continue to Constrain Capital Inflow

Recently, the National Bureau of Statistics published its Capital Importation data for Q2:2023. On a year-on-year (YoY) basis, total Capital Imported dipped by 32.90% to USD1.03bn in Q2:2023 compared to USD1.16bn imported in Q2:2022. This reflects significant decline in two of its major components, Foreign Direct Investment (-41.54% YoY to USD86.03mn) and Foreign Portfolio Investment (-85.89% YoY to USD106.85). However, its third component, Other Investment (+32.73% YoY to USD837.34mn) increased in the period.

On a quarter-on-quarter (QoQ) basis, the story remains unchanged as total Capital Imported fell by 9.04%, following an 83.54% QoQ plunge in FPI. However, we note that the growth in FDI (+80.71% QoQ) and Other Investment (+92.16% QoQ) helped to minimize the QoQ decline in total capital imported.

Figure 1: Capital Importation by Type of Investment



Source: NBS, ARM Research

Foreign Direct Investment: Momentous QoQ Surge

Foreign Direct investment (FDI) in Q2:2023 declined by 41.54% YoY to USD86.03mn, underpinning continuous deterioration in foreign investors' appetite for long-term investments in Nigeria, as it has been the trend since Q1:2022. Structural imbalances (Insecurity, infrastructure deficit, FX illiquidity) have continued to permeate the Nigerian economy counteracting the government's efforts towards attracting FDI. However, on a QoQ basis, FDI surged 80.71%, the first uptick since Q4:2022. Consequently, FDI contribution to total capital importation grew by 4.15% to 8.35% in Q2:2023.

Foreign Portfolio Investment: Dwindling Inflow

In Q2:2023, Foreign Portfolio investment (FPI) dipped by 85.89% YoY to settle at USD106.85mn (vs. USD757.32mn in Q2:2023). This is attributed to foreign investors wariness to invest in Nigeria due to its underlying political and economic uncertainties. Furthermore, persistent hawkish monetary policy measures adopted by developed economies present opportunities for investors for strong positive real returns, further deterring FPI inflow. However, optimism emerged, albeit only short-lived, following actions by the President Bola Tinubu led Administration to unify the foreign Exchange rate and end fuel subsidies. On a QoQ basis, FPI dropped by 83.54%. This is alluded to a decline in Equity (-96.17% QoQ), Bond (-71.67% QoQ) and Money Market Instrument (-89.64% QoQ) investments. Also, FPI contributed 10.37% of the total capital imported in the Q2:2023 (vs. 57.32% contributed in Q1:2023).

Other Investments: Fuelled by Increased Loans

The Other Investment category rebounded in Q2:2023 as it grew by 32.73% YoY and 92.16% QoQ respectively to USD837.34mn (vs. USD630.87mn in Q2:2022 and USD435.76mn in Q1:2023). Unsurprisingly, Loans made up a major part of this category, accounting for 92.14% of Other Investment. Hence, we attribute the significant QoQ increase in Other Investment to the 77.82% QoQ surge in Loans to USD771.53mn (vs. USD433.87mn in Q1:2023).

Sectors with Highest Capital Importation

The production sector had the highest inflow of capital in Q2:2023 with USD605.04mn, contributing 58.73% to the total capital imported, outrunning the banking sector. The banking sector followed with USD194.58mn, contributing 18.89% (a decline from 26.89% in Q1 2023). The telecoms sector contributed USD25.81mn (2.51%), and the financing sector contributed USD63.77mn (6.19%). The recent scarcity of FX in the country aided the decline of the banking sector despite the FX unification policy introduced.

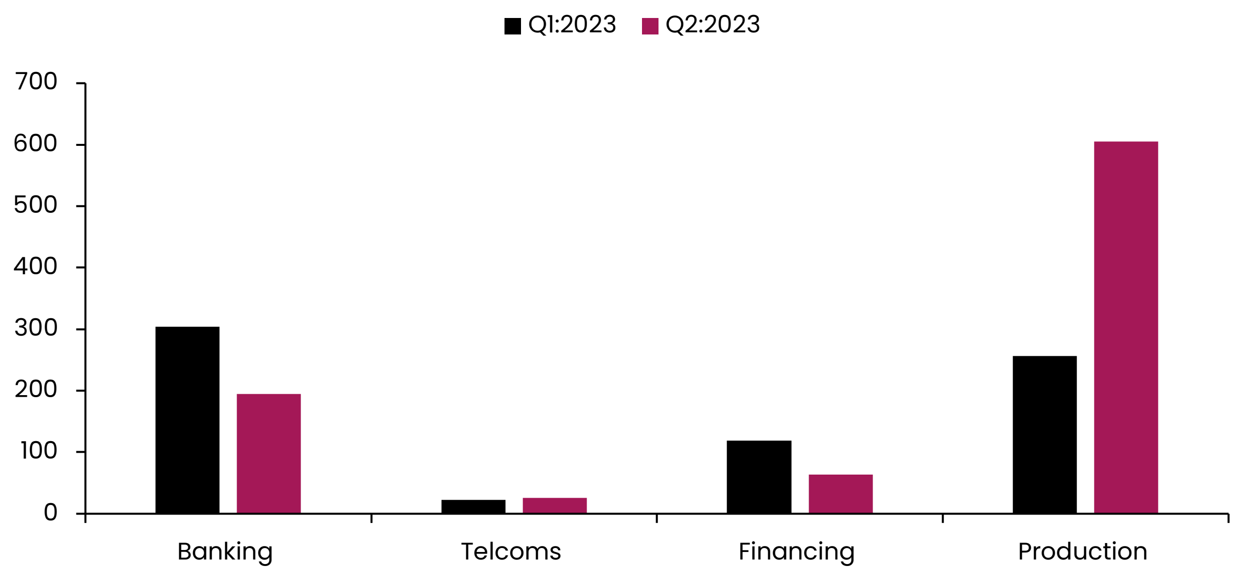
Capital Importation by Country of Origin

The top countries that funded Nigeria's capital importation were the United States USD271.92mn, Singapore USD177.44mn, the Republic of South Africa USD136.95mn, the United Kingdom USD131.49mn, and the United Arab Emirates USD101.13mn. The top three (3) countries accounted for 26.39%, 17.22%, and 13.29% of the total capital inflow, respectively.

States with Highest Capital Importation

Lagos State had the highest capital inflow USD778.06 million, followed by Abuja (FCT) with USD194.28mn, Akwa-Ibom state with USD33.86mn, Ogun State with USD24.00mn and Ekiti State with USD0.01mn. Lagos state and Abuja (FCT) both contributed 75.52% and 18.86% of the total capital inflow respectively.

Figure 2: Capital Importation by Sector (Q1:2023 vs. Q2:2023)



Source: NBS, ARM Research

Outlook for Q3:2023 – Same Tricks, Same Results

Q2:2023 was largely characterized by a change in political administration with the transition into the new Nigerian Presidency. Shortly after the inauguration, the government enacted pro-market policies, which were positively received by investors. However, these failed to materialize into sustainable drivers of growth, underpinning the structural inefficiencies.

Despite the liberalization, and subsequent convergence of the multiple foreign exchange (FX) windows regime in June 2023, the unabated pressure on foreign reserves with strong FX demand led to a renewed disparity between the official and parallel market rates.

For clarity, shortly before the rate convergence, the Importers' and Exporters' (I & E) rate was quoted at NGN471.67/USD on the official market and the parallel market rate at NGN760.00/USD or a NGN288.30 (61.13%) premium. In months following the FX policy, and as of 9th October 2023, the I & E rate was quoted at NGN741.85/USD (vs. parallel market's NGN1,004/USD) or a NGN262.15 (35.34%) premium.

To address the FX challenges, an overhaul of the previous CBN administration led to the appointment of Dr Yemi Cardoso as the new CBN governor, thus indicating a possible shift back to orthodox monetary policy.

The current investment landscape does not prove favourable for international investors, as indicated by the decline in FDI over the years. We opine that current trends will subsist over the next quarter; underscored by the low FX liquidity, uncleared FX forward backlogs (c. USD6.8bn), and the weak accretion of improved oil production levels to foreign reserves.