Flashnotes

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Prospect for Attaining 6% Average Growth Rate in 4 years

Highlights

- **The World Bank has retained its 2023 GDP growth forecast for Nigeria at 2.80% which it says is barely above the population growth rate and accordingly too slow to address the challenges of extreme poverty in the country.**

- **The president, during his inauguration speech had set target to increase the GDP growth rate of the country by 6% on average in the next 4 years through budgetary reforms aimed at stimulating the real sector of the economy.**

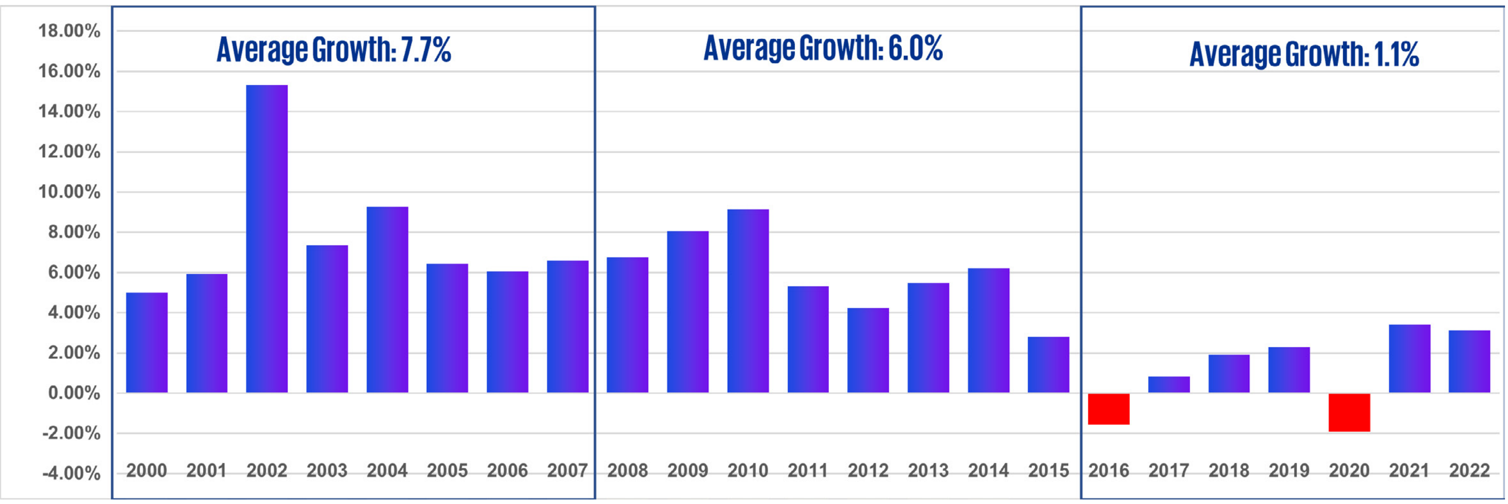
- **An average GDP growth rate of between 4-4.5% at the best is more feasible in the next 4 years. Even this will require the country to get its policies right and keep consistent faith with macroeconomic reforms.**

Event

The World Bank retained its 2023 GDP growth forecast for Nigeria at 2.80% from 3.3% recorded in 2022. This 2023 forecast is in line with KPMG's revised forecast of 2.85% (from 3.0% earlier stated), following the release of Nigeria's Q1 2023 GDP estimates last month. In its statement, the World Bank postulated that Nigeria's growth which has averaged about 1.5% in the last decade was too slow to address the challenges of extreme poverty in Nigeria due to high inflation, the naira redesign cash crunch in Q1 2023 and low foreign exchange availability. According to the World Bank, growth in Nigeria is expected to remain barely above the population growth rate which is far slower than needed to make significant inroads into mitigating extreme poverty.

Analysis/Opinion

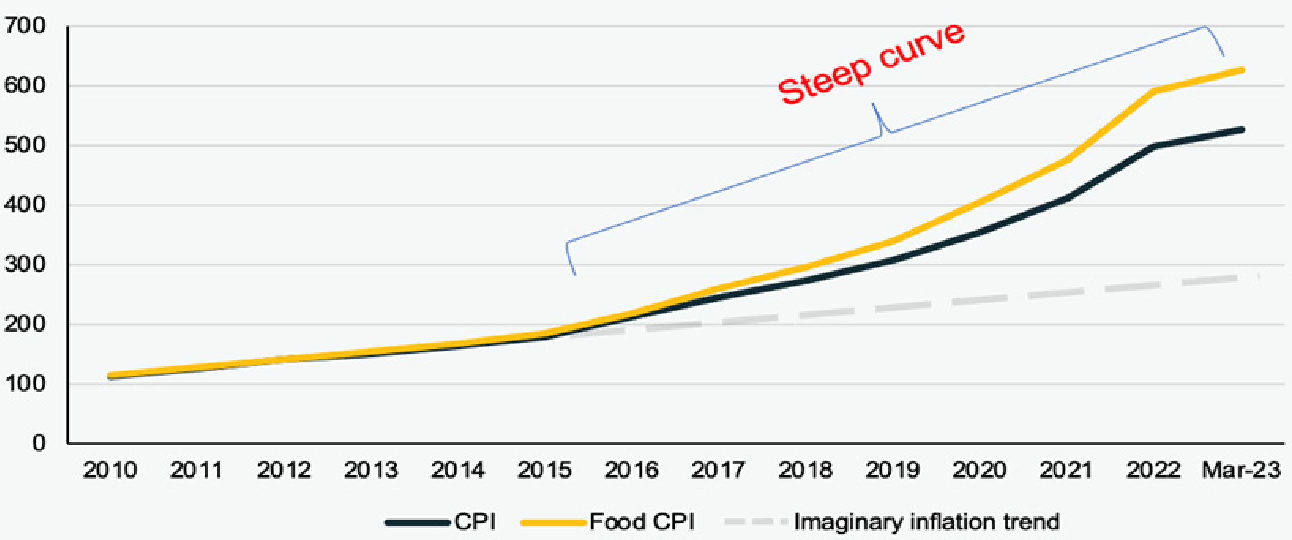
The role of economic growth in reducing poverty is well recognized especially if the benefit of that growth is adequately distributed. Nigeria's growth since 2019, has been fragile, not growing fast enough to contain population growth (2.6%-3.0%) and needs to be less inequitable (with a Gini coefficient of 35.1% in 2022). Accordingly, per capita income has contracted by over 40% since 2015.



The fact that Nigeria's GDP will need to grow by at least 6% to generate enough jobs to absorb labor market growth (about 4% per annum) and reduce poverty is well understood by President Tinubu's Administration. The president, during his inauguration speech had set target to increase the GDP growth rate of the country by 6% on average in the next 4 years through budgetary reforms aimed at stimulating the real sector of the economy.

However, we are of the opinion that this might be difficult to attain in four years. For example, the consensus among analysts is a GDP growth in 2023 of between 2.7-3.2%. Thus, if we assume a GDP growth of 3% in the first year, the economy will then have to grow by an average of 7% for the subsequent 3 years and moving growth from a forecasted 3% in 2023 to at least 7% in 2024 and afterwards seems overly ambitious. At the same time attaining a 6% real GDP growth on average from 2023 to 2026 means growing the value of real GDP from N74.6 tn in 2022 to N92.5tn by 2026 representing an increase of N17 trillion in 4 years. However, within 12 years, 2010 and 2022, real GDP grew by about N17 trillion which will have to be replicated in just 4 years and within a much more challenging macroenvironment that cuts across the fiscal, monetary, external, and real sectors.

End Period Consumer Price Index (CPI)



Three key areas with higher CPI change than overall CPI

	Category	Percentage change from 2010 to 2023Q1
1.	Food	443%
2.	Food and Alcoholic Bev	438%
3.	Imported Food	389%
	Overall CPI (All items)	**361%**

GDP, using the expenditure approach, is the cumulation of household and government consumption expenditure, private and public investment, and net exports which means the president will have to introduce policies and take decisions that will lead to growth across these variables. However, taking decisions in one variable can lead to a decline in another. For example, to grow government revenue to expand government consumption and investment, it might increase taxes and /or borrow from the private sector. However, increasing taxes can lower purchasing power and slow consumption expenditure growth. At the same time private investment may be curtailed as business earnings are squeezed from slowing demand, higher costs from higher taxes and higher interest rates as government borrowing crowds out private sector lending and then pushes rates up. The ability to maintain a fine and delicate balance across these variables will be important. But where will the required 6% average growth needed to meet the president's, target come from?

As of end of 2022, we estimate the following breakdown of GDP by expenditure.

Strategies to create growth: Expenditure Model

C + I + G + X - M

Real Consumption

- Household Consumption (69%) N51tn

Real Investment (I) PI+GI

- 23% (N17tn) of which...
  - Private Sector Investment (59%) N10tn
  - Government Investment (41%) -N7tn

Real Government Expenditure (G)

- Government Consumption Expenditure (7%)N6tn

Real Exports (X)

Real Imports (M)

X-M=1% N1tn

The economy will need to grow an additional N17trillion in 4 years through these components of GDP.

Household consumption expenditure which is the largest share of GDP and the easiest to grow is however constrained by high double digit inflation which is expected to get worse with the subsidy removal, the implementation of the finance bill 2022 and the unification of the FX rate whenever it is implemented within the next 4 years, in addition to the perennial supply and transportation bottlenecks, security concerns and power and other infrastructural constraints to doing business in Nigeria which tend to put pressure on costs of production and price of goods and services. The latest VAT data from the FIRS for example shows an annual growth in nominal VAT collected in 2022 of 21%. However, average inflation in 2022 stood at 19% suggesting a real growth of about 2%.

Real GDP Billions 2010-2022		
Year	**N' trillion**	**Year on Year Growth N' Trillions**
2011	57.5	2.9
2012	59.9	2.4
2013	63.2	3.3
2014	67.1	3.9
2015	69.0	1.9
2016	67.9	-1.1
2017	68.4	0.5
2018	69.8	1.4
2019	71.3	1.5
2020	70.0	-1.3
2021	72.3	2.3
2022	74.6	2.3
Needed by 2026	**92.5**	**4.4/average per annum**

Private investment which accounts for the second largest share of GDP is also limited by the high inflationary environment and the weakness in consumption expenditure. It is also constrained by the increase in finance costs with the CBN raising MPR from 11% to 18.5% and this high interest rate environment is expected to remain in the short to medium term. The sectors expansion is also constrained by the overall high cost of operations as well as supply and transport bottlenecks and power challenges. The initiatives government and the private sector may also have to put in place to cushion the effects of the removal of petrol subsidies may also worsen the costs of businesses and leave less for expansion in the short to medium term which covers the duration of the president's first term and the focus of his growth targets.

Net exports are currently characterized by crude oil export which still account for most of total exports having challenges with production which has now been capped by OPEC. With respect to non-oil exports, it has not grown sufficiently due to challenges in production of its main export product, crude oil, and is unlikely to grow sufficiently in the next few years given continuous production challenges in the sector and the recent OPEC+ quota on output at 1.38mbbd. At the same time non-oil exports are unlikely to record any dominate performance in the short to medium term as all the factors that need to be fixed for this to happen will take a longer period to be effective. At the same time import demand is set to continue especially as border controls and import restrictions are relaxed. With exports unlikely to rise substantially in the short to medium term and imports not likely to slow, growth in net exports will also be difficult. Accordingly, the governments major short-term growth strategy will therefore be to boost government investment and government expenditure (accounting for about 15% of GDP combined) to attempt to unlock the potential of the private sector and stimulate domestic consumption and exports. It may therefore have no option than to borrow more and/or increase tax collection given the low fiscal space and despite the already high debt and debt service environment of above 50% even after subsidy removal. This may however constrain GDP growth in the short term by squeezing households and businesses, this further indicates that 6% on average in 4 years is unlikely.

In conclusion, while we expect stronger year on year growth over the next few years, we are of the opinion that there is very limited space to attain a 6% average real growth rate in 4 years or an increase in real GDP by N17trillion. We are of the opinion that an average GDP growth rate of between 4-4.5% at the best is more feasible in the next 4 years. Even this will require the country to get its policies right and keep consistent faith with macroeconomic reforms.

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