



الوكالة الإسلامية الدولية للتصنيف  
Islamic International Rating Agency

# ECONOMIC & BANKING SECTOR OVERVIEW

**Federal Republic  
of Nigeria**

*December, 2020*

## Economic Overview

Nigeria is expected to face multiple challenges as it recovers from the COVID-19 induced disruptions. A higher than expected fiscal deficit, decline in exports, lower oil prices, currency depreciation and in turn higher inflation continue to pose economic stress in 2020 and 2021.

At 200mn, Nigeria is the most populous African country. The economy is largely dependent on oil and gas sector, and has suffered a setback with the most recent oil price shock in 2020, with the onset of the Covid-19 pandemic. With a nominal GDP of USD 446.5b and 1.7% real GDP growth during 2019 (2018: 1.9%), the economy is performing below potential, since the previous oil price slump in 2015-2017. Nigeria was expected to grow at a higher pace of 2.5% during 2020, however, the on-going pandemic has put the economy into recessionary conditions, expected to shrink by 3.4% in 2020 and gradually recover to post an expected growth of 2.5% in 2021. Much remains uncertain, with a continued slump in the global economy and trade, keeping oil prices below sustainable levels and reduced optimism for complete recovery before 2022.

The economy is faced with various long standing structural challenges which foster economic vulnerabilities with more than half of the population subsisting below the poverty line, extremely high unemployment, and inflationary conditions. Inflation has remained in double digits, although gradually moving down to 11.4% in 2019 from a high of 16.5% in 2017. As COVID-19 caused supply disruptions, inflation rose to 12.82% as of August'2020, its highest in 27 months, despite dwindling economic demand. The Central Bank of Nigeria decreased the policy rate to 11.5% after two consecutive cuts in 2020, from 14% in 2018 and 13.5% in 2019. The currency has also remained weak with the Naira falling from N307/\$ before COVID19, to N380/\$. With considerable downside volatility in oil price and a weak long-term prognosis in the present scenario, we expect Nigeria to remain vulnerable on the external account. The outbreak of the pandemic has also accelerated capital flow reversals, which continues to stoke fears of further local currency devaluation against USD.

Nigeria's fiscal dependence on oil is noteworthy. As such fiscal deficit of 5% to GDP in 2019 is likely to grow beyond 6.5% in 2020, given current price environment. Further, the government took various measures to address the challenges imposed by COVID-19 including announced packages for health spending and issuing a revised budget with NG 500b (0.3% of GDP) COVID-19 intervention fund, which puts further pressure on the fiscal account.

## BANKING SECTOR

The penetration of the banking sector has been on a rising trend where unbanked population has reduced from ~41.6% in 2016 to ~36.8% in 2019. Nigerian banking sector spans 22 conventional banks and 2 non-interest banks with Jaiz Bank being the first such bank. With total assets of NGN 41.9trn in Dec-2019, Nigeria's banking sector has grown at a 3 year CAGR of ~9.8% (2016-2019).

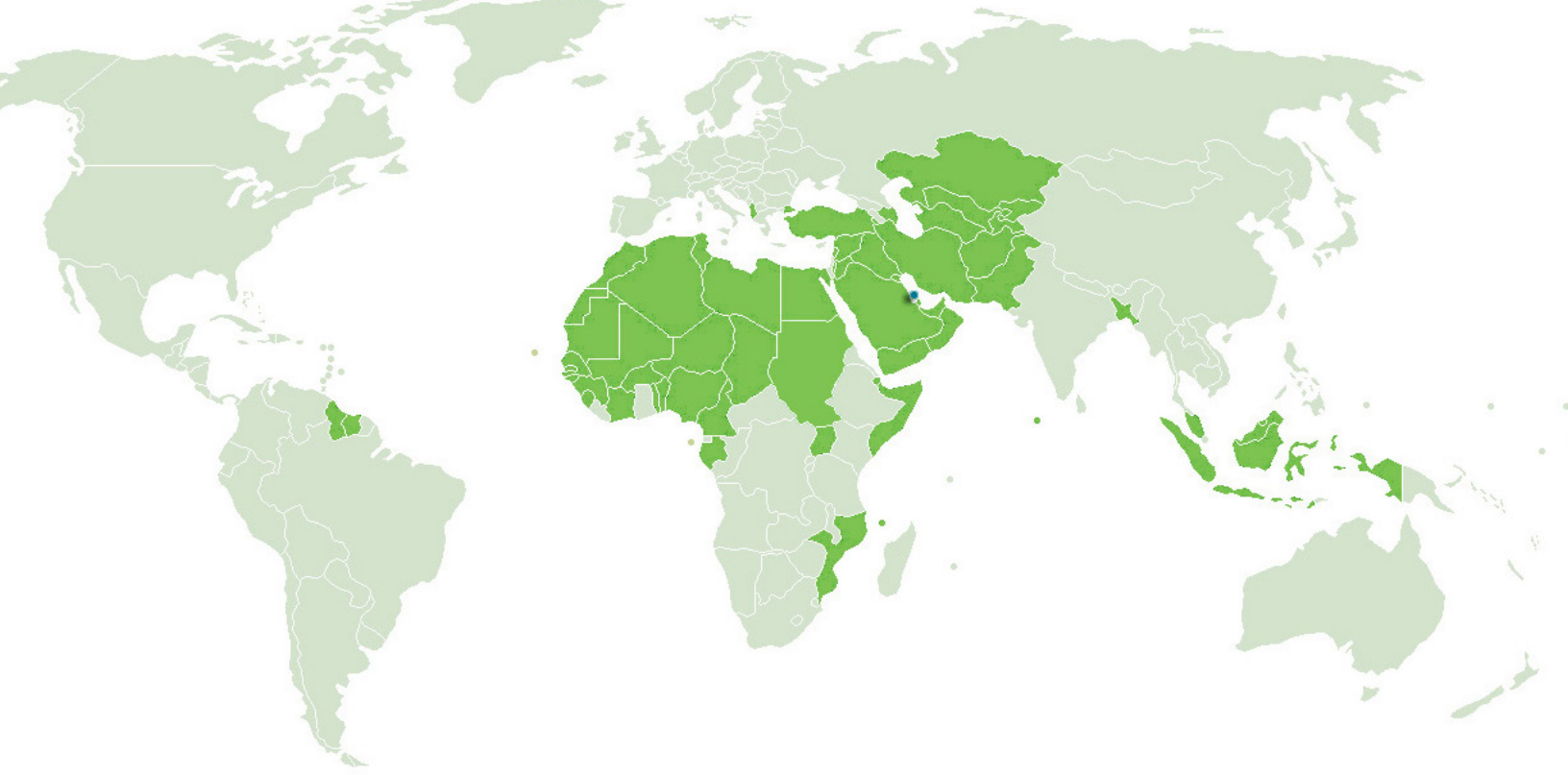
	2016	2017	2018	2019
Population (million)	184.0	189.0	195.9	200
GDP per capita (USD)	2,206	1,995	2,049	2,235
GDP (USD bn)	405	376	397	447
Real GDP growth	-1.6	0.8	1.9	1.7
Unemployment Rate	13.40	17.50	22.60	-
Fiscal Balance (% of GDP)	-4.0	-5.4	-4.3	-5.0
Public Debt (% of GDP)	19.60	23.40	28.40	29.0
Inflation Rate (CPI, annual variation in %)	15.70	16.50	12.10	11.4
Policy Interest Rate (%)	14.00	14.00	14.00	13.5
Exchange Rate (vs USD)	304.50	305.50	306.50	360.0
Current Account (% of GDP)	0.70	2.80	1.0	-3.8
International Reserves (USD)	27.60	39.80	43.60	38.1
External Debt (% of GDP)	12.9	17.5	19.0	18.3

Source: IMF Consultation report 2020

The industry has been hit by credit crisis in prior years peaking most recently in 2015-2017 oil price shock resulting in non-performance, spiking from 2.3% in 2014 to 14.0% in 2016 and dropping significantly by end 2019 to 6.1%. While potentially faced with heightened credit risk in the present scenario, the low loan to deposit ratio in the industry, along with lower concentration in riskier segments including oil and gas, real estate and construction, power and Energy and Transportation which fell to ~40.6% of total financing in 2019 as against an average of ~45.1% between 2014-2018, may contain overall risks. Strong pre-provision profitability of the banks has also provided significant cushion to absorb potential asset quality deterioration. Moreover, the CBN has extended a moratorium to borrowers in specific loan categories in the face of the pandemic.

Nevertheless, downside risks to the sector are pertinent in the prevailing scenario. The CBN has by directive imposed a minimum loan to deposit ratio of 65% in September 2019, raised from 60% as set in July 2019, to push lending to the private sector. Increased cash reserve requirement on the shortfall in lending as a penalty of non-compliance is likely to serve as an incentive to financing growth. The CBN's efforts to direct lending to strategic sectors continues, including the most recent directive issued in September 2020, to increase lending to the agricultural sector. While this induces credit growth in the economy on the one hand, enhanced stress on repayment capacity of borrowers on the other, may result in impairment charge-offs to surge in the sector in 2020 and 2021.

Successive interest rate cuts may also suppress banks' margins in 2020. Stressful macroeconomic challenges like expected contraction in real GDP coupled with further expected devaluation of currency may expose banks to foreign currency liquidity challenges and potential foreign exchange losses, despite reduction in net foreign currency assets of the industry over the last reported period. On the whole the banking sector is likely to face stress on earnings, with an increased need to enhance buffers in the sector's balance sheet.



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P.O. Box 20582, Kingdom of Bahrain  
Tel: +973 17211606, Fax: +973 17211605  
Website: [www.iirating.com](http://www.iirating.com) | Email: [iira@iirating.com](mailto:iira@iirating.com)

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