

# Falling Oil Prices and Implications for Nigerian Capital Markets

A presentation

by

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## Outline

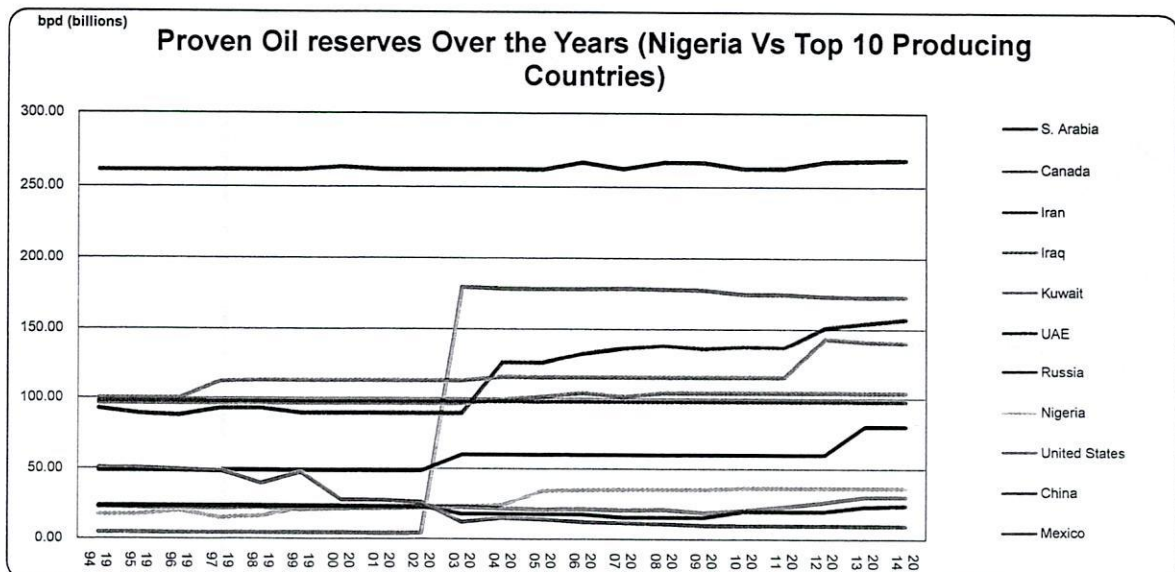
- Introduction
- Why do we have lower oil prices at this time?
- Implications of oil Price Fall on Nigeria
- Impact of lower oil prices on capital Markets
- Conclusion

## Introduction

- Opec's 12-member group has largely controlled the global price of crude oil for the past 40 years, but the US's discovery of shale oil and gas has dramatically shifted the balance of power
- A sudden plunge in the price of oil is sending economic and political shockwaves around the world
- Oil exporting countries are bracing for potentially crippling budget shortfalls and importing nations are benefiting from the lowest prices in four years.
- The global price of oil is near \$83 per barrel, down about \$32, or 28 percent, from its high point for the year
  - ✓ As Opec's % of worlds oil production is falling

## Introduction

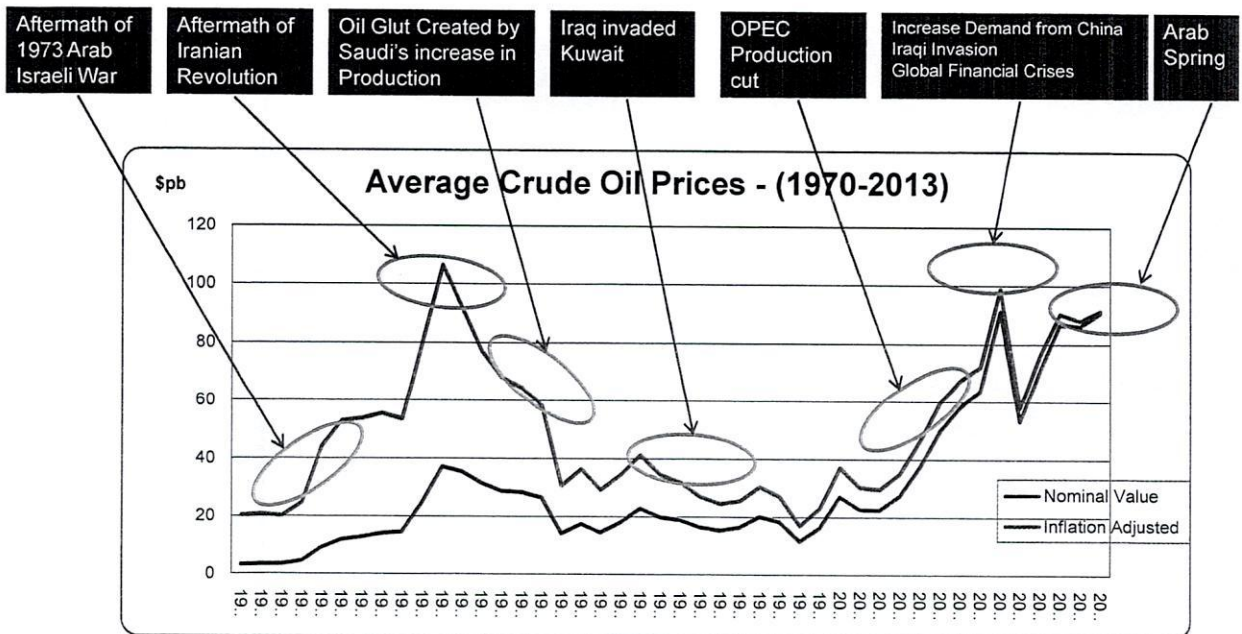
**Proven Reserves of top 10 Producers Over the Years - Nigeria's proven reserves has remained untapped over the years**



# Introduction

# Introduction

## Oil Price Movement Over the Years



## Introduction

- Oil consumption globally is 91 million barrels per day down from a peak of 92.7 million barrels per day midyear
- The drop can be associated with the impact of new technology that relies less on oil and the discovery of Shale gas in the US
  - ✓ That means the world's oil producing countries and companies are bringing in as much as \$2.8 billion less in revenue every day
  - ✓ Resulting in consumers, shippers and airlines e saving a comparable amount on gasoline, diesel and jet fuel.

## Why do we have lower oil prices at this time?

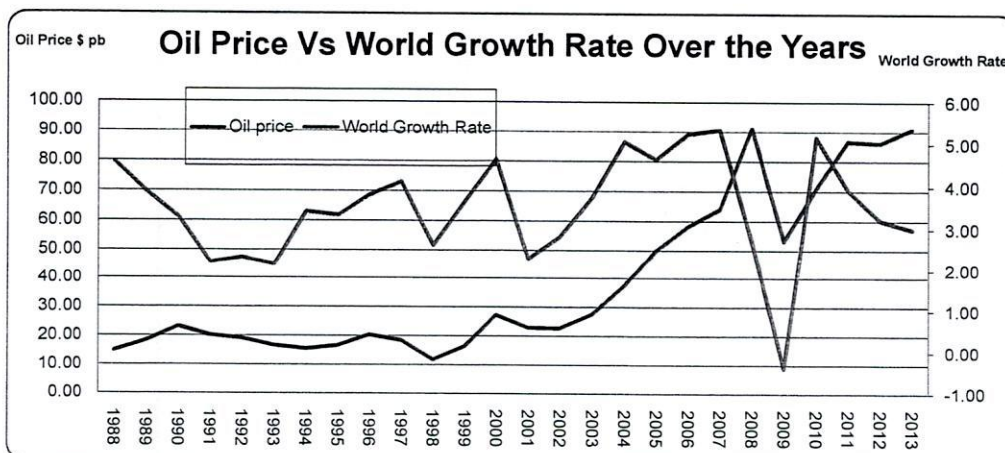
- The global price of oil was relatively stable for nearly four years, averaging \$110 per barrel
- Increased production in the U.S., Canada, Iraq and elsewhere made up for declining supplies in nations such as Iran and Libya and helped meet rising global demand
- That delicate balance has been upended by a weaker global economy
  - ✓ Demand is slowing while production, particularly in the U.S., continues to surge
- In general the plunge in prices is good for those who have to buy fuel, and bad for those who sell it
- But it has far wider and more complex effects on economies around the globe that are only starting to be felt.

## Why do we have lower oil prices at this time?

- Saudi Arabia, the world's largest exporter and OPEC's most influential member, might not rush to cut production
  - ✓ However, even though it would start running a deficit with oil at \$85 per barrel, according to Merrill Lynch
  - ✓ With a large reserve fund -- estimated to be \$700 billion -- it could withstand a longer period of lower prices.

## Impact of Lower Oil Prices on Global Economies

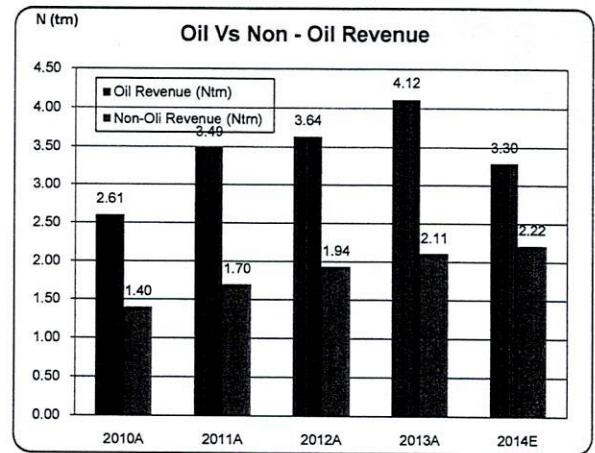
- Rising oil prices appear to have a negative effect on global growth prospects
- As oil prices rise through the years world growth seems stunted as energy costs increase in non oil producing industrialised countries



## Implications of oil Price Fall on the Nigerian Economy

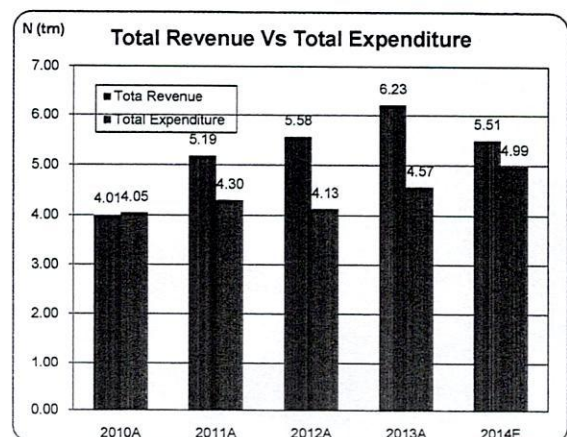
### Oil Price to Government Revenue

- Oil revenue peaked at N4.21 trillion in 2013
- Given recent developments in the oil markets we anticipate a 20% decline in oil revenue for 2014
- This would be compounded by the activities of militants in the Niger Delta and oil thieves
- We do not anticipate a significant increase in non oil revenue to make up for the shortfall



## Implications of oil Price Fall on Nigeria

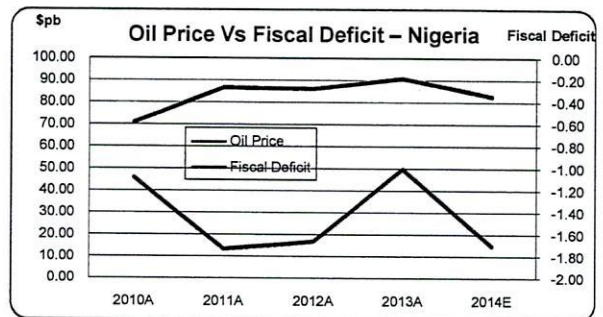
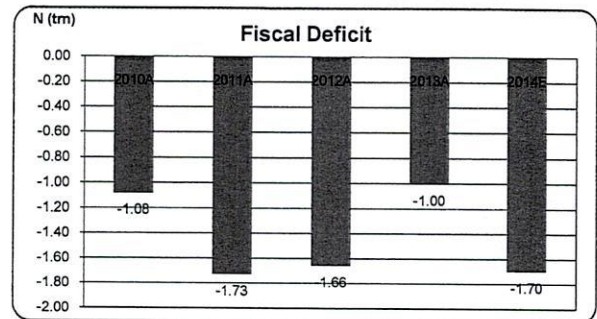
- Federally collectable revenue peaked in 2013 owing to healthy oil prices
- This is expected to dip in 2014 despite higher expenditure profile
- It should be pointed out that federally collected revenue services the following areas
  - ✓ Monthly statutory allocations
  - ✓ Debt service (domestic and foreign)
  - ✓ Accretion to the external reserves
  - ✓ Commitments to JV partners
  - ✓ Funding of SWF



## Implications of oil Price Fall on Nigeria

### Oil Price to Interest Rates

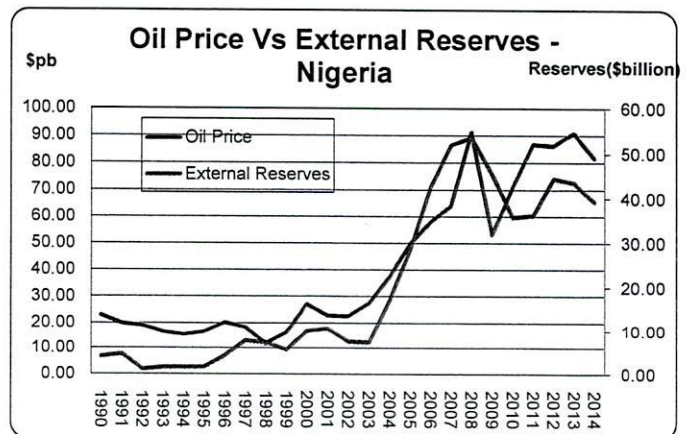
- With the shortfall in oil revenue hence - overall government revenue - fiscal deficit will likely rise from N1 trillion in 2013 to around N1.7 trillion in 2014
- Higher fiscal deficit will translate into higher government borrowing
- Higher government borrowing would result in higher interest rates



## Implications of oil Price Fall on Nigeria

### Oil Price to Exchange Rates

- 90% of governments forex earnings is generated through oil sales
- Lower oil revenue will have implications for forex earnings
- With lower forex earnings accretion to external reserves becomes challenging
- More than likely government would continually drawdown on the reserves weakening its position
- Lower external reserves would lead to a weaker Naira as it is one of Naira's key fundamentals
- Exchange rate of the Naira would thus deteriorate



## Implications of oil Price Fall on Nigeria

### Oil Price to Stock Market

- The relationship between prices on the stock market is indirect and would manifest through the following channels

#### Interest Rates

- Interest rates becomes high as government borrowing increases
- High interest rates would make fixed income instruments more attractive to the investors
- This would gradually sucks liquidity from the stock market to the fixed income market

#### Exchange Rates

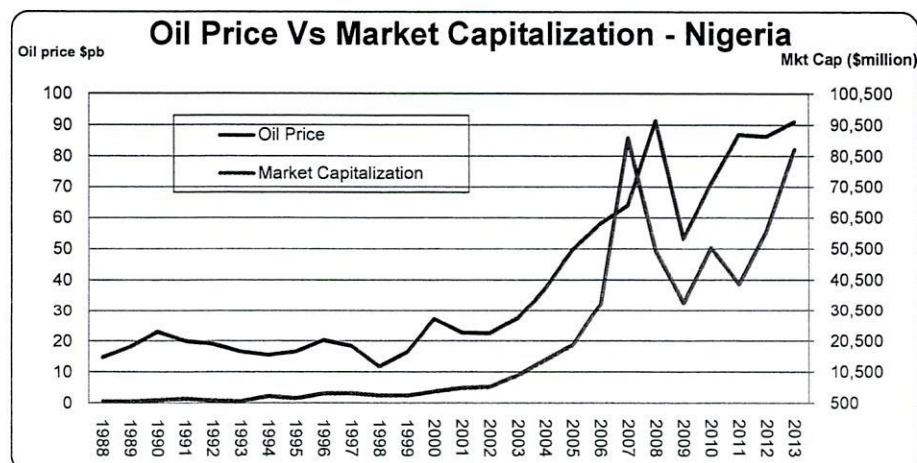
- A weakened exchange rate would prompt foreign portfolio Investors to:
  - sell down their positions
  - switch currencies to mitigate against exchange rate risks
- A massive sell down would lead to depressed stock prices

#### Oil Consuming Economies

- Liquidity would likely move to oil consuming markets which would have improved economy due to lower oil prices
- As such economies improve their financial markets would also improve

## Implications of oil Price Fall on Nigeria

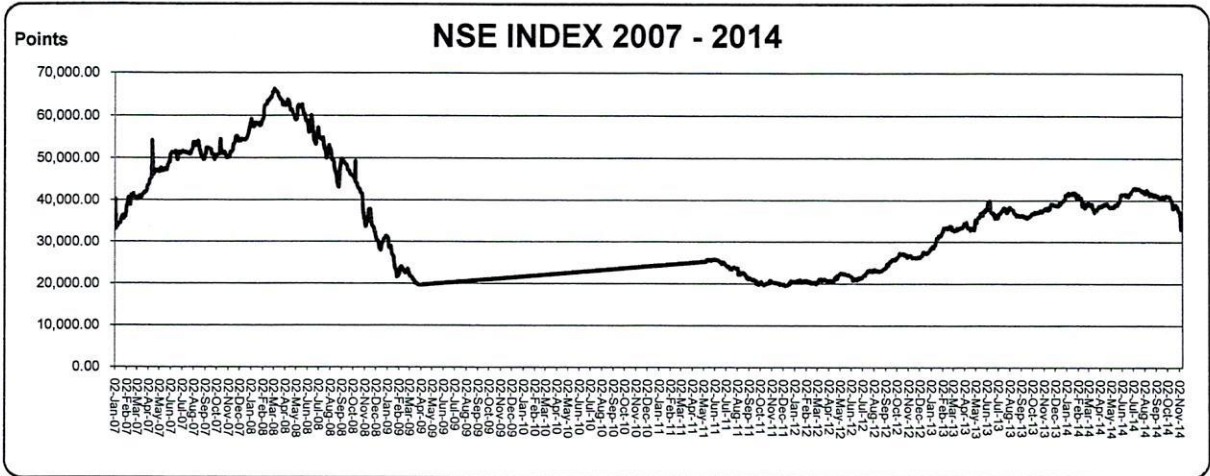
- Market Capitalization has grown in tandem with oil prices over the years





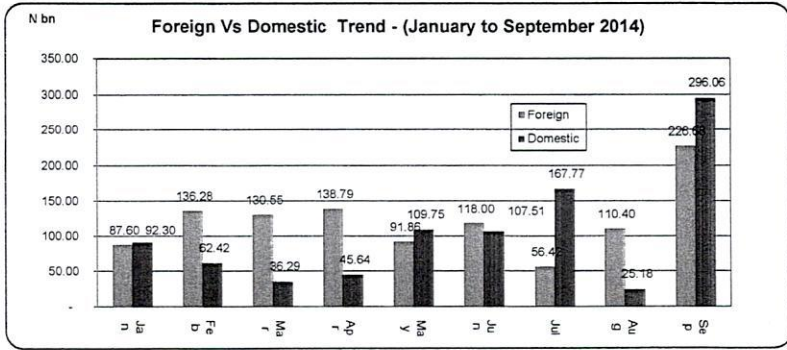
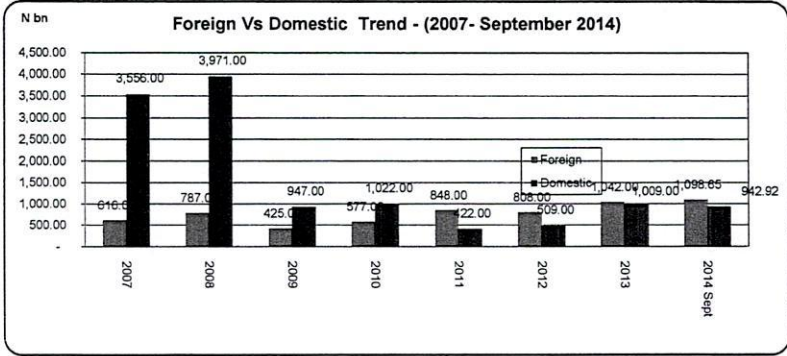
# Implications of oil Price Fall on Nigeria

- NSE ASI peaked at over 65,000 points in 2008 before retreating to less than 20,000 points at the height of the meltdown in 2009
- The highest it has done since then is just 42,000 points in July 2014

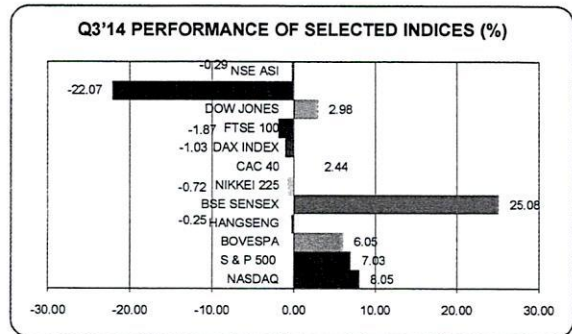
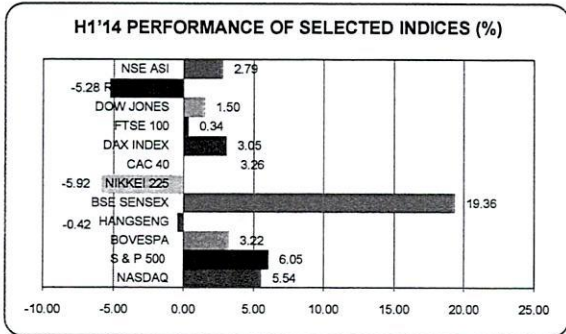
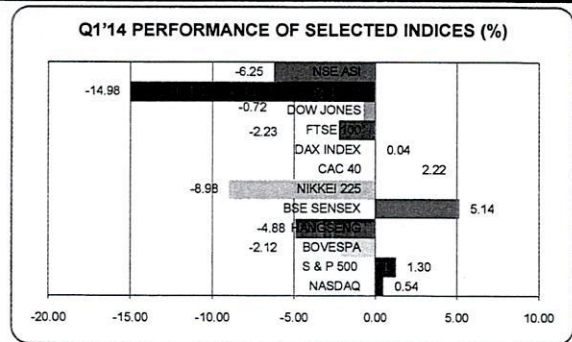
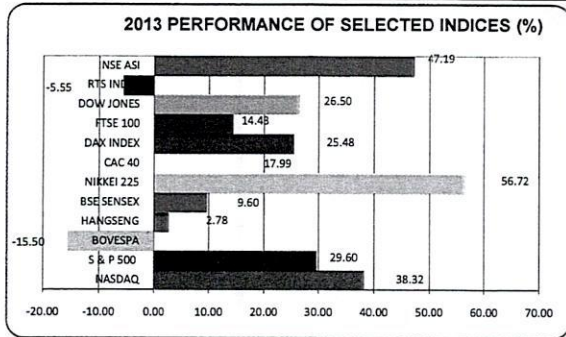


# Implications of oil Price Fall on Nigeria

- Foreign portfolio investments in the Nigerian capital market peaked in 2011 and peaked in 2013
- Foreign investors dominated the market until the tide started turning in September

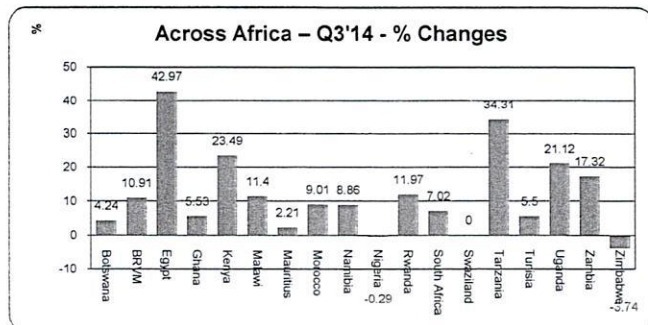
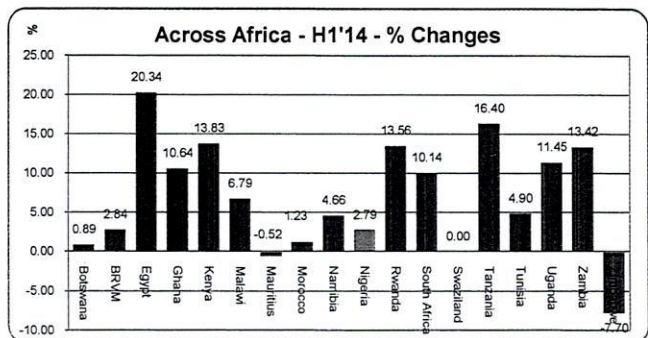


## Review of Market Performance in Q3 2014



## Review of Market Performance in Q3 2014

- Egypt tops African market in Q3'14 with 42.97% gain
- Followed by Tanzanian and Kenyan Markets
- Nigeria is one of the least rewarding markets in Africa in Q3
- ✓ Second to Zimbabwe



## Conclusion

- Falling oil prices will impact negatively on Nigerian government revenue
- Oil consumers are expected to gain as oil gets cheaper as this translate to improved economies
- Lower oil prices will also have serious implications for interest and exchange rates in Nigeria
- Falling oil prices would have an indirect but haemorrhaging effects on the stock market through deteriorating exchange and interest rates
  - Higher interest rates is bad for equities as liquidity could be drawn away from the equities market to the foxed income market
  - Exchange rate deterioration would serve as a disincentive to foreign portfolio investors who may sell down their stock positions and switch currencies to hedge against exchange rate risks
  - Both actions would lead to depressed stock prices