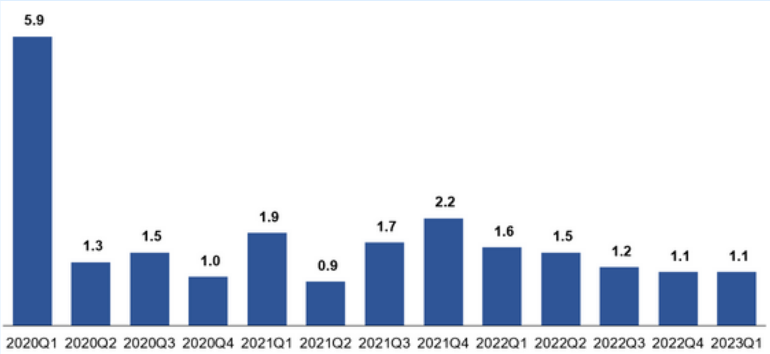
NESG 2023Q1 CAPITAL IMPORTATION ALERT

July 2023

Overall investment inflows into Nigeria plunged by 31 percent (year-on-year) in 2023Q1

According to the National Bureau of Statistics (NBS), foreign investment inflows declined to US$1.1 billion in 2023Q1 from US$1.6 billion in the corresponding period of 2022 (see **Figure 1**). However, on a quarterly basis, the overall investment inflows remained unchanged. Weakening foreign investment inflows suggests the persistently high-risk aversion towards investing in Nigeria by foreign investors.

Figure 1: Trend of Foreign investment inflows (US$ billion)



Data: NBS; Chart: NESG Research

Annualised decline in all components fuelled the drop in overall foreign investment inflows. The decline in foreign investment inflows in 2023Q1 was driven by a fall in the values of the three (3) components of capital importation: **Foreign Portfolio Investment** (FPI), **Foreign Direct Investment** (FDI) and **Other** investment. Nonetheless, the disaggregation of capital importation remains biased towards FPI, which accounted for 57 percent of total inflows in 2023Q1, down from a 61 percent share recorded in 2022Q1 (see **Figures 2a and 2b**). Also, the share of FDI dropped to 4 percent in 2023Q1 from 10 percent in 2022Q1. However, the share of "Other" investment rose to 38 percent in 2023Q1.

Figure 2a: Composition of Investment inflows in 2023Q1 (percent)

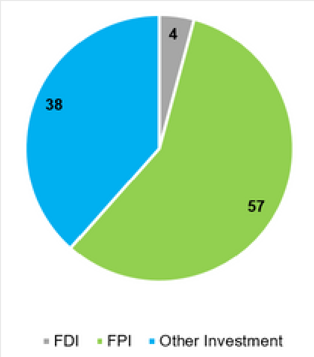
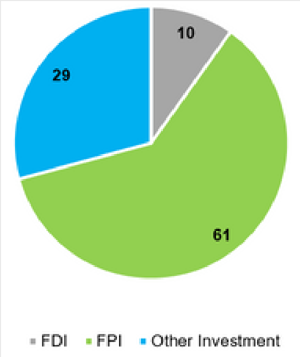


Figure 2b: Composition of Investment inflows in 2022Q1 (percent)

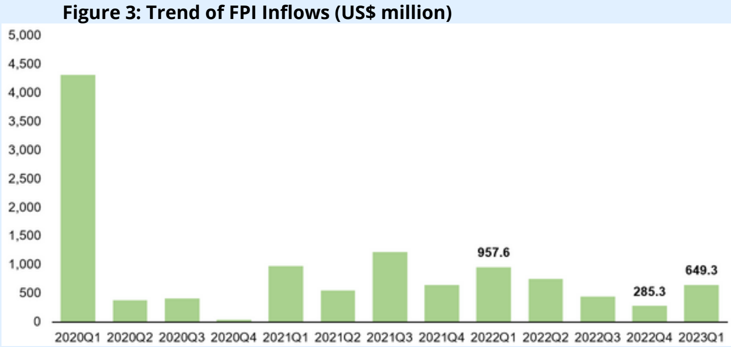


Data: NBS; Chart: NESG Research

FPI inflows dropped by 32 percent (year-on-year) in 2023Q1. Total FPI inflows in 2023Q1 stood at US$649.3 million, which is 32.2 percent below US$957.6 million recorded in 2022Q1 (see **Figure 3**). A further breakdown of the FPI shows subdued uptake of Nigerian equities among foreign investors. According to the Nigerian Stock Exchange (NGX) Limited, the participation of foreign investors in the equities market fell sharply to 4 percent in 2023Q1 from 23 percent in 2022Q1[1]. The decline in FPI reflects investors' apprehension arising from foreign exchange shortage, negative real returns on investment, and challenges in repatriating funds abroad. Meanwhile, there was an astronomic increase in FPI on a quarter-on-quarter basis, attributable to the waning political risks surrounding the 2023 General Elections.

[1] see Foreign Portfolio Investment Reports for March 2022 and March 2023, retrieved from: https://ngxgroup.com/exchange/data/foreign-portfolio-investment-report/

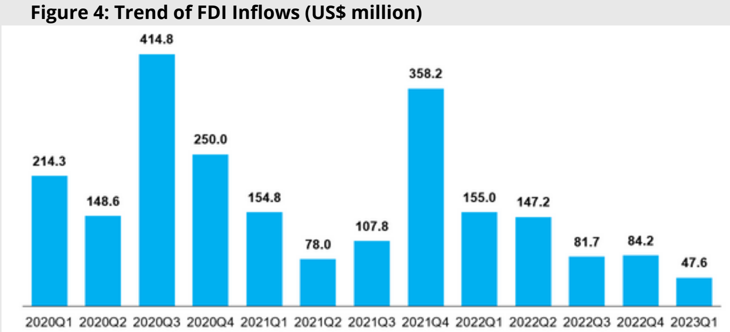
Figure 3: Trend of FPI Inflows (US$ million)



Data: NBS; Chart: NESG Research

FDI inflows fell by more than two-thirds in 2023Q1. Foreign Direct Investment (FDI) – the most stable source of investment flows – stood at US$47.6 million in 2023Q1, which is 69.3 percent (year-on-year) lower than US$155 million recorded in 2022Q1 (see **Figure 4**). Remarkably, Nigeria has, over time, lagged behind its regional peers, such as South Africa and Egypt, which remain Africa's first and second-largest recipients of FDIs. The inability of Nigeria to attract a substantial portion of the global FDIs could be attributed to various challenges, including foreign exchange scarcity and difficulty in profit repatriation, insecurity, infrastructural deficit, and regulatory bottlenecks, among others.

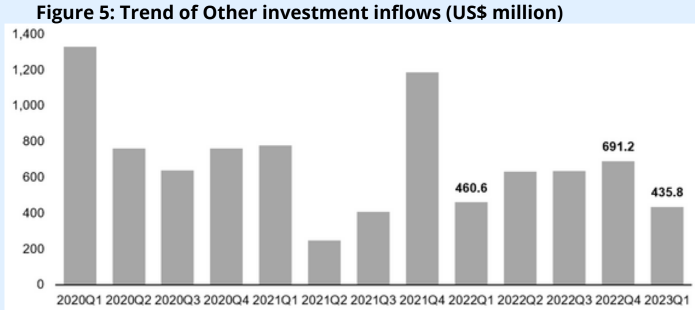
Figure 4: Trend of FDI Inflows (US$ million)



Data: NBS; Chart: NESG Research

"Other" Foreign Investment Inflows fell slightly (year-on-year) in 2023Q1. Similar to FDI and FPI, the value of Other categories of foreign investments - covering foreign loans, trade credits, currency deposits and other claims - declined by 5.4 percent to US$435.8 million in 2023Q1 from US$460.6 million in 2022Q1 (see **Figure 5**). In terms of composition, foreign loans almost accounted for nearly 100 percent of Nigeria's other categories of foreign investment in 2023Q1.

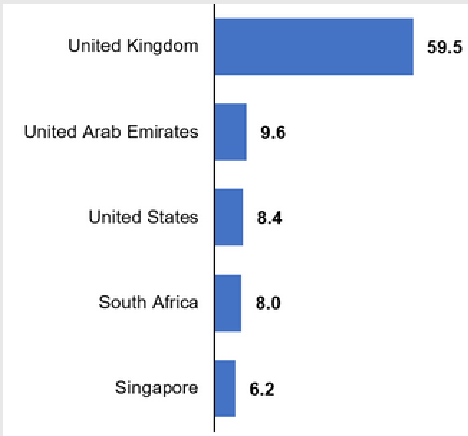
Figure 5: Trend of Other investment inflows (US$ million)



Data: NBS; Chart: NESG Research

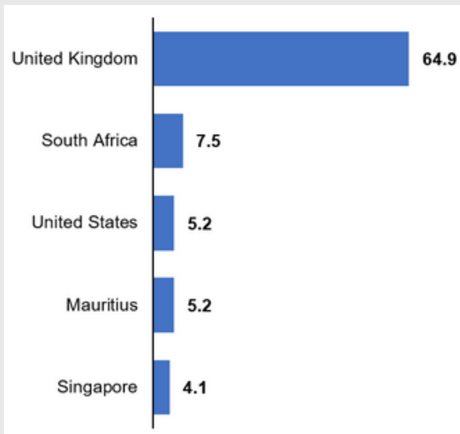
United Kingdom remains Nigeria's largest source of foreign investments. The United Kingdom maintained its position as the largest source of investment inflows into Nigeria, accounting for 59.5 percent of the total inflows (equivalent to US$673.6 million) in 2023Q1. Countries, including the United Arab Emirates, the United States, South Africa, and Singapore, also featured among the top five (5) investment sources, accounting for a combined share of 32.2 percent in the quarter. South Africa is the only African country that has consistently contributed significantly to foreign investment inflows into Nigeria (see **Figures 6a and 6b**).

Figure 6a: Capital Importation by Origin (Percent share of Total) – Top 5 in 2023Q1



Data: NBS; Chart: NESG Research

Figure 6b: Capital Importation by Origin (Percent share of Total) – Top 5 in 2022Q1



Data: NBS; Chart: NESG Research

Lagos and Abuja are the major investment hotspots in Nigeria. Accounting for a share of 62 percent in overall investment inflows in 2023Q1 (US$704.9 million), Nigeria's commercial epicentre – Lagos - maintained its position as Nigeria's most attractive investment destination. Similarly, FCT-Abuja remained the second largest investment destination at 36 percent of the total investment inflows (US$410.3 million) in the quarter. Moreover, nine (7) states led by Akwa Ibom accounted for the remaining 1 percent share (US$17.5 million) in 2023Q1.

Foreign-affiliated banks largely facilitated foreign investment inflows in 2023Q1. In 2023Q1, twenty-one (21) banks facilitated the inflow of foreign investments into Nigeria. About 85 percent of the total inflows (US$963.1 million) were facilitated by four (4) foreign-affiliated banks, while Nigerian-owned banks facilitated the remaining 15 percent of total inflow (US$169.5 million) in the quarter.

CONCLUDING REMARKS

* **The buckets of pro-market reforms by the current administration are expected to stimulate the inflows of FDI in the coming quarters.** The recent removal of fuel subsidies and the liberalisation of the foreign exchange (FX) market are historic, as such the reforms signal market clarity and reduce information asymmetry, which helps unlock foreign investment inflows. Meanwhile, to reap the full gains of these reforms, there is an urgent need to address the issue of FX scarcity and difficulty in fund repatriation abroad.

* **The unification of exchange rates allows foreign portfolio investors to become less vulnerable to currency speculation risks.** The previously managed float regime is characterised by distortions emanating from inappropriate FX pricing and multiple FX windows. These factors constitute a disincentive to foreign investors and give room to currency speculators to take advantage of the parallel market premium. Efforts should, therefore, be geared towards improving FX availability through non-oil sources of FX such as non-oil exports and foreign remittances.

* **The harmonisation of exchange rates could reduce the country's attractiveness to foreign loans.** The FX reform is expected to elevate the value of Nigeria's external debt stocks and external debt servicing. The debt service to revenue ratio reached an all-time high of 101.5 percent in December 2022 (World Bank)[2]. This gives no room for excessive external borrowing, considering that the country still struggles to grow fiscal revenues.

[2] see World Bank's Nigeria Development Update for June 2023, retrieved from: https://reliefweb.int/attachments/b0d0cf63-00c1-4119-9d53-ecd23983ff8b/EN.pdf

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