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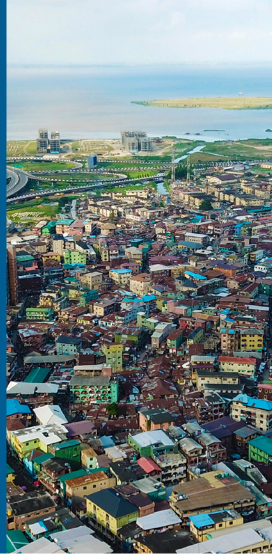

Tales From the Emerging World

Nigeria's New Dawn?

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Nigeria, often described as the "Giant of Africa," is perhaps the world's largest country that investors know the least about. We believe that may soon change given demographic trends and a potential uptick in economic growth. On our recent visit we observed both the adverse consequences of policies implemented by the prior administration and the potential opportunities offered by the promise of change as a new president takes control.

Nigeria suffered eight years of economic stagnation under the administration of the previous president, Muhammadu Buhari, a former general who had promised to tackle corruption. According to the World Bank the country ranked among the top 15 fastest-growing economies globally between 2001 and 2014, with an average growth rate of 7%. But the economy careered off the rails during Buhari's two terms, starting in 2015, with annual real GDP growth averaging a paltry 1.4% during his tenure.

Buhari's failure to remove fuel subsidies and the implementation of foreign currency controls hobbled the private sector, while a lack of economic growth exacerbated the level of extreme poverty. Today, some 71 million people live below $1.90 a day, a significant jump from 61 million in 2016. By contrast, most countries have reduced their poverty levels significantly - India saw a decline from 74 million people in poverty to 44 million. During Buhari's tenure the average Nigerian saw their annual income shrink by nearly one-third, from $3,222 to $2,200, one of the steepest declines recorded by any country over that time span, while Kenyans saw their incomes rise by more than 40% (*Display 1* - see following page).

Not surprisingly, many Nigerians chose to flee during Buhari's reign. According to UN data, Africa's most populous nation witnessed its biggest-ever net migration of people over any eight-year span. "Japa," a Yoruba term meaning "to run away or escape," has entered the general lexicon, spawning influential social media accounts providing advice for leaving, and influencing popular Afropop songs.

Then came the election of Bola Tinubu in 2023. Few had high expectations that the political insider could bring about meaningful change despite his success as the governor of Lagos State from 1999 to 2007. Yet, as

Ken Opalo, a political scientist at Georgetown University noted, Tinubu was able to put Lagos on "a gradualist path to prosperity" and improve public services, by persuading an enormous number of people who had shirked paying taxes to start doing so. Reviving the fortunes of Nigeria's commercial center may yet serve as a template for the country's future success.

From the start Tinubu appeared to be in a hurry to tackle the policies that had hindered economic growth. During his inaugural address in May, the new president declared that the "Fuel subsidy is gone." Nigeria, Africa's largest oil producer, had spent vast sums subsiding gasoline prices since the 1970s. Scrapping the subsidy, which cost a whopping $10 billion in 2022, could free up funds for schools and hospitals. But Nigerians, who had grown accustomed to pumping cheap gasoline, saw fuel prices triple overnight.

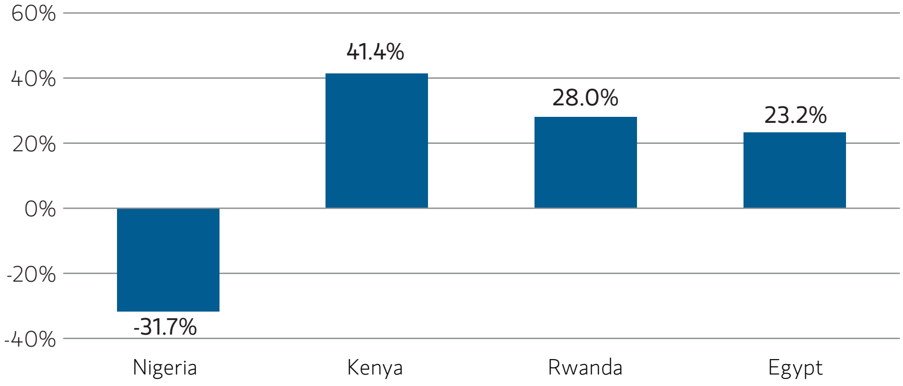
The president next targeted the country's overvalued and complex currency regime. While the official exchange rate was pegged at Nigerian Naira (NGN) 460 to the U.S. dollar (USD), the unofficial market rate traded at a significantly higher rate of NGN 750. Multiple exchange rates had prevented foreign investors from repatriating money out of Nigeria and deterred most from investing new capital into the country. In June, Tinubu ordered the immediate reunification of the rates, in effect depreciating the currency by 67% (*Display 2*), and suspended the Central Bank of Nigeria's governor—widely viewed as the architect of the multiple foreign-exchange rates policy.

The removal of subsidies is likely to prove painful in the near term, especially as it will likely erode consumer confidence, send inflation higher and hurt consumption. We believe Tinubu's actions could potentially mark a turning point and deliver medium-term growth which will spur the emergence of a mass consumer market in one of the fastest growing populations in the world.

DISPLAY 1

Nigeria's Economy Has Been in Reverse Gear Under Buhari

Change in GDP per capita in USD from 2015-2022



Source: Haver Analytics.

As incomes rise, the demand for many consumer products typically rises even higher, as goods become affordable, exhibiting an "S-curve" of consumption. To cite one well-known example, when GDP per capita in China rose from $1,000 to $4,000, the demand for automobiles rose at an even greater rate, from one million vehicles to over 17 million.

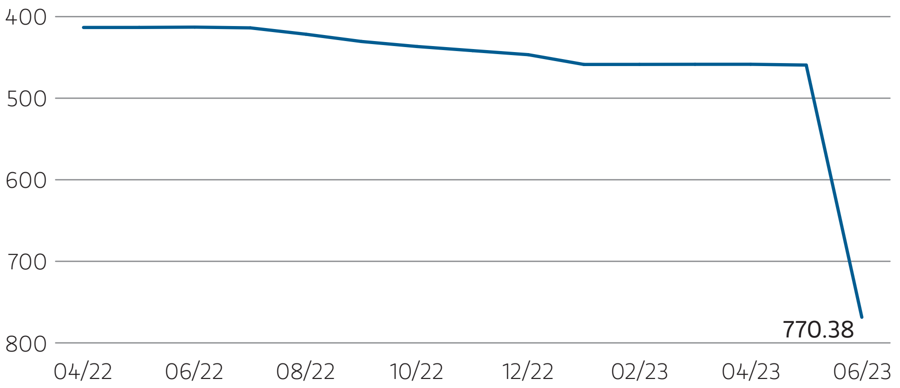
Nigeria currently has a population of 223 million and will add another 38 million to its labor force over the next decade, more than any other country other than India. More consumers mean more demand for consumer products, including apparel, branded fast-moving consumer goods and even durables. About half of the population—a staggering 110 million—is 17 or younger. The size of this tech-savvy generation, raised in an era of expanding internet connectivity and smartphones, is likely to fuel strong growth in cellular data consumption.

That should benefit telecom operators who can now enter the mobile-money market in a country where around 55% of the population have no bank accounts. More than 85% of the adult population in Nigeria

DISPLAY 2

An End of Currency Bands Causes the Biggest Drop in Nigerian Naira (NGN)

NGN/USD, EOP (Inverted)



Source: Haver Analytics, Bloomberg. As of June 2023 have a mobile phone but only 10% have a mobile-money account, much lower than the 75-95% penetration seen in Senegal, Ghana and Kenya. We therefore think mobile banking will be an attractive investment opportunity in the coming years.

Delivering economic development will be key. High investment and rapid industrialization, often viewed as pathways to economic prosperity for emerging economies, have proven difficult for all but a handful of developing countries. Nigeria is probably not going to replicate East Asia's manufacturing success anytime soon, but perhaps it could do more to boost services exports. By some estimates, 125 million Nigerians speak English which is more than the populations of the UK, Canada and Australia combined. A large pool of English speakers is an asset which underpins successful service export industries including the Philippines Business Process outsourcing (BPO) sector, which generates more than $35 billion a year in hard currency. We would urge the new administration to focus on investments in educational outcomes and skill development, everything from improving too-low literacy rates, to prioritizing STEM fields. Bridging the gap in outcomes between the North and South of the country will be key, but we can think of no better use for the $10 billion in annual savings from fuel subsidies.

We tend to agree with Nandan Nilekani, co-founder of Infosys, when he said, "People who travel to emerging markets like India or Nigeria often see only the problem of a billion hungry mouths. What they miss are the billion minds, and the potential of those minds." The new administration's challenge is to devise sound policies to unleash the potential of Nigeria's human capital, perhaps its greatest asset. The reforms are a positive step but more needs to be done to ensure momentum is not lost. Tinubu and his team of technocrats have a unique opportunity to free up the economy and attract foreign investors looking for sustained growth.

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