

FDC Economic Bulletin

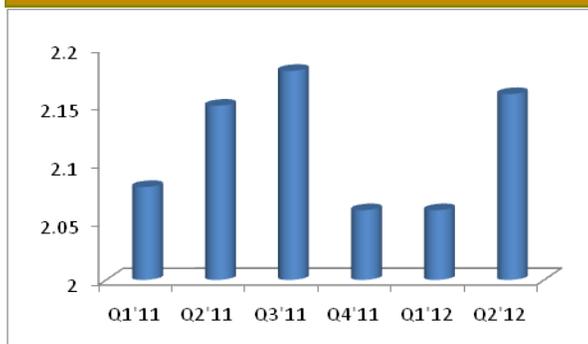
August 2012



Jump in Crude Oil Production - Is this Nigeria's Finest Hour?

Nigeria's crude oil production spiked to an all-time high of 2.7mbpd on the 25th of July, the first time in 50years. This peak represents an increase of 28.57% from the year-to-date average of 2.11mbpd. The

Chart 1: Nigeria's Crude Oil Production (mbpd)



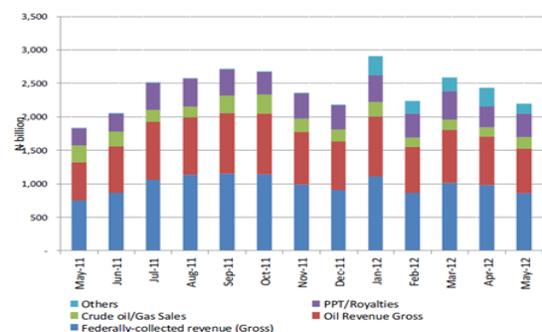
Source : OPEC

Group Managing Director of the Nigerian National Petroleum Corporation (NNPC) attributed the hike to a sharp reduction in oil theft. Oil theft and pipeline vandalism (or leakages), is a fall out of the Movement for the Emancipation of the Niger Delta (MEND) struggle for resource control and environmental protection. The after math of the struggle has resulted to the much-needed security measures put in place by the Federal Government in the Niger Delta region.

Nigeria's Oil Purse Leaks...

The annual loss from these leakage activities is approximately \$5bn or 7% of total government revenue to leakages such as oil theft. The Niger Delta, Nigeria's major oil producing region (contributing 70% of total production), is relatively at peace after years of militant attacks, truce and now almost a lasting solution. The amnesty program implemented earlier by late President Yaradua for MEND members was a huge success with an attendant improvement in crude oil production to 2.1mbpd from the average of 1.86mbpd pre amnesty declaration in 2009. The gains were however reversed due to the activities of illegal bunkering and oil theft. With the new record production level of 2.7mbpd the question is: is this spike sustainable?

Chart 2: Gross Oil Revenue and its Components



Source : CBN

How Sustainable is it?

The increased security measures mentioned above have helped boost production. However, the threat of

a resurgence in MEND attacks and further attacks on pipelines make this level seem unsustainable. The government will need to intensify efforts to maintain high production levels through increased and tighter security measures, repair and maintenance of refineries, and a timely passage of the Petroleum Industry Bill (PIB).

How sensitive is the Nigerian Economy to Higher Crude Oil Production?

Oil receipts, a function of oil price and productions, account for approximately 80% of government revenue. Our regression model shows that government revenue is more sensitive to oil production than oil prices. Increased oil production will therefore have greater impact on the government's finances and the attainment of its fiscal and monetary goals. The Federal Government's 2012 budget is benchmarked to an oil production of 2.4mbpd as against the new record production of 2.7mbpd. According to the CBN, government revenue declined by 12.3% from N974.8bn to N855.1bn in May, as a result of an 8.2% decrease in oil receipts. This loss in oil receipts was attributed to a drop in oil and gas sales during the month. Moreover, oil output fell from 2.18mbpd to 2.13mbpd in May. What, then, will be the implications of a higher production level on the Nigerian economy?

Implications of an Increased Oil Production Level on Nigeria

Using our regression model, at a monthly average production level of 2.4mbpd (65% likelihood based on current trends), we estimate a 6.06% increase in government revenue to N906.9bn in September, a 4.56% increase in forex inflows to \$3.85bn and an accretion in Nigeria's external reserves to \$45bn-covering 9months of imports. At an average production level of 2.7mbpd (a 35% likelihood), we estimate a 10.7% increase in government revenue to N946.97bn, a 9.12% rise in forex inflows to \$4.02bn and reserves accretion to \$60bn-covering over 10months of import cover. Resultantly, the CBN may allow the naira to appreciate sharply to N145/\$1, to compensate for the substantial increase in oil revenue.

Outlook

We believe the outlook for Nigeria's crude oil production is positive. The combined effect of the relative peace in the Niger Delta region and the likely passage of the PIB will result in an increase in oil production, above the current trend of 2.1mbpd on average, in the short run. We forecast an average production of 2.45mbpd for the rest of the year. The impact of this will be an increase in oil revenue by 20%, an accretion in external reserves to \$42.5bn, and a reduction in fiscal deficit to an estimate of 2.5%. The overall impact will be a sharp appreciation in the naira to N152-153/\$1.

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