

February 11, 2019

*(N.B. Due to the President's Day holiday, the next report will be published February 25.)*

### **The Nigerian Election**

On February 16, 2019, Nigeria will hold its sixth presidential election since it ended military rule in 1999. President Muhammadu Buhari, who has been rumored to be in bad health after disappearing from public view for weeks at a time, is facing a serious challenge from the former vice president, Atiku Abubakar. Although there are several other challengers, their chances of winning are slim.

In a country where presidents typically serve two terms, Buhari appears vulnerable to being removed from office after his first. In a word, his first term can be described as turbulent. The economy fell into recession, there were bouts of fuel scarcity and his health troubles sparked rumors that he had been replaced by a Senegalese body double.<sup>1</sup> In 2016, even his wife registered her discontent with his performance by insinuating that she may not support him in his re-election bid. Recent actions by Buhari and his government suggest he has not taken his declining popularity in stride. As a result, there is growing concern that the election could become violent.

Even though the last election saw a relatively peaceful transition of power, historically, elections in Nigeria have been violent. Thus, this election has garnered international attention as it could possibly

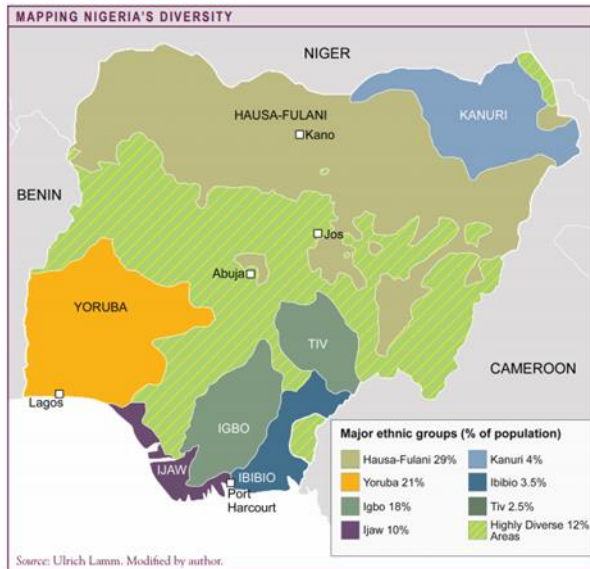
lead to broader conflict within the region. While we are concerned with the humanitarian aspects of this event, the primary focus of this report will be on how the election could impact financial and commodity markets. We will examine the overall political situation in Nigeria, the issues surrounding recent elections and the potential for unrest following the vote. As always, we will conclude with potential market ramifications.

### **Brief History of Nigeria**

Nigeria is located in West Africa and has the continent's largest population and economy. It is the largest oil producer in Africa and the 7<sup>th</sup> biggest supplier of oil to the U.S. Due to its size and scope, Nigeria has outsized influence in regional affairs and is widely considered the prominent power in Africa. This is seen in its pronounced role in multilateral organizations such as the Economic Community of West African States (ECOWAS) and the African Union.

As a result of the country's past as a former British colony, it remains split along religious, tribal and geographical lines. Nigerians who live in the north are predominantly Muslim and are part of the Hausa or Fulani tribes. In the southwest, Nigerians are split between Christians and Muslims and generally come from the Yoruba tribe. The southeastern region is predominantly made up of Christians generally from the Igbo or Ijaw tribes. There are other groups that follow traditional religions within Nigeria but they represent a minority. In total, there are over 400 different ethnic groups in Nigeria. Ethnic differences between these groups are a key source of political tension.

<sup>1</sup> <https://www.wsj.com/articles/on-the-issue-of-whether-ive-been-cloned-an-election-gets-weird-1544459732>



(Source: Africa Center for Strategic Studies)

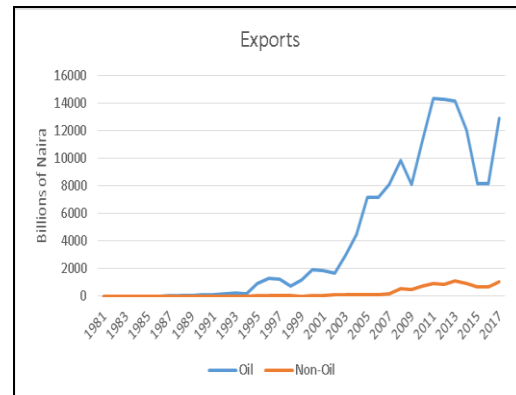
The northern region has had disproportionately more power over the southern region as the military is primarily headquartered in the north. Furthermore, though the nation’s capital was located in the southwestern city of Lagos until 1991, almost all heads of state were from the northern region. As a result, people living in the south have accused the north of using their political clout to steal from them; most of the country’s mineral resources are in the south. In order to quell unrest, there is a general agreement between the north and south that the presidency will switch every two terms.

**The Resource Curse**

Nigeria’s economy has diversified over the past few years but it still depends heavily on exports of oil and natural gas. Despite oil and natural gas comprising only 10% of its total output, these resources account for about 60% of the government’s revenue and 92% of export earnings.<sup>2,3</sup> As a result,

<sup>2</sup><https://www.cbn.gov.ng/Out/2018/RSD/CBN%20ECONOMIC%20REPORT%20THIRD%20QUARTER%20%20%202018%20published.pdf>

Nigeria’s economy has a lot of exposure to oil prices and the dollar.<sup>4</sup>



(Source: Central Bank of Nigeria)

Despite being the 8<sup>th</sup> largest exporter of oil in the world, Nigeria still remains one of the world’s poorest nations by GDP. Although the country is resource rich, it struggles to build up industries besides oil, which is typical of countries with a single resource. The discovery of oil in Nigeria led to the suppression of other industries as the strengthening exchange rate made other Nigerian goods less competitive. As a result, oil exports wildly outpace exports of other goods as the chart above shows. Nigeria’s dependence on oil means its economy is quite vulnerable to oil price changes. This phenomenon is referred to as the "resource curse" and is not unique to Nigeria as almost every country in OPEC suffers from this problem.

The lack of diversification within the Nigerian economy has hindered the government’s efforts to raise the living standards of its citizens. A common symptom of the resource curse is that the resulting currency appreciation makes goods abroad relatively cheaper than goods produced domestically; consequently,

<sup>3</sup>[https://www.cbn.gov.ng/Out/2018/SD/2017%20Statistical%20Bulletin\\_External%20Sector\\_Final.xlsx](https://www.cbn.gov.ng/Out/2018/SD/2017%20Statistical%20Bulletin_External%20Sector_Final.xlsx)

<sup>4</sup> Oil trades in dollars

domestic industries suffer. In order to protect domestic industries the government has relied on import substitution industrialization (ISI). This policy involves the government intervening in the economy by limiting imports through tariffs and quotas and using state funds to invest in projects and boost consumption. ISI has had mixed success and has ultimately led to high levels of inflation due to state-funded industries never learning efficiency.

Because the Nigerian government generates most of its revenue from oil rather than taxes, citizens do not really have much of a voice in establishing policy. Therefore, patron-client relationships are commonplace within the government. State oil funds are generally funneled to those with the most connections and can afford to pay bribes and sponsor candidates. In this environment, the right person elected into office can be life-changing. This is why groups that lose elections resort to violence as a way to ensure the government meets their needs. For example, in 2016, a militant group called the Niger Delta Avengers terrorized parts of south Nigeria until it was given a share of oil revenue.

### **Election**

Since defeating Goodluck Jonathan, a southerner, in 2015, Buhari has struggled to maintain his popularity. During his first term, he suffered through health scares, a recession and a revitalized threat from Boko Haram, now known as Islamic State West Africa Province. His political adversary, Atiku Abubakar, a former supporter who hails from the north, is seen as a legitimate challenger in this month's election.

Nigeria has a multi-party system that is dominated by two major parties, the All Progressive Congress (APC) and the People's Democratic Party (PDP). The

incumbent, Buhari, is a member of the former, and his opponent is a member of the latter. These two parties have a duopoly in Nigerian politics that has limited the number of options for Nigerians to choose from. For example, Buhari has been the APC candidate for the last five elections. Abubakar of the PDP served two terms as vice president from 1999 to 2007.

The stakes are high in this year's election as each candidate vies for different patronage networks. Annual oil production fell 26% from 2007 to 2017, according to the Energy Information Agency. Although some of this drop can be attributed to terrorism along the delta, there is speculation that some oil fields are depleted. How to solve this problem is at the heart of electoral tensions. There are two sides: one side favors privatizing the oil industry to help attract foreign investment, while the other side favors keeping the industry in state hands. The former supports Abubakar, while the latter supports Buhari.

Many of Abubakar's supporters backed Buhari in his original bid for the presidency. In 2018, Buhari angered many of his supporters by refusing to sign a bill to privatize portions of the state oil company.<sup>5</sup> In his defense, Buhari claimed the bill would have undermined his role as president and oil minister.<sup>6,7</sup> He went on to accuse proponents of the bill of pushing privatization to put money in the hands of the corrupt. With both sides openly feuding, there have already been accusations of political censorship and political arrests. Earlier this month, military officials raided

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<sup>5</sup> <https://www.ft.com/content/8da566ac-1a46-11e9-9e64-d150b3105d21>

<sup>6</sup> Buhari appointed himself as oil minister, a possible conflict of interest.

<sup>7</sup> <https://www.ft.com/content/3d785448-c71f-11e8-86e6-19f5b7134d1c>

offices of the *Daily Trust*, a popular newspaper critical of the military, on the grounds that stories published by the newspaper put national security at risk.<sup>8</sup> Within days of the raid, a judge was suspended for corruption allegations moments before he was to swear in members of the Elections Tribunal, a group that could decide the election if it is close.

The two challengers have done little to mitigate tensions between the two sides as each has accused the other of rigging votes and inciting violence. Opponents of Buhari believe his appointment of his daughter-in-law, Amina Zakari, to the head of the Independent National Electoral Commission's collation center is a clear signal that he is trying to rig the vote. At the same time, Abubaker's opponents claim he is encouraging Islamist militants in the north to stir up violence in order to suppress voting. Although such accusations are not unusual, hostility has risen between the two camps as the election approaches. Last week, the PDP, the party of Abubakar,

threatened to withdraw from a national peace accord after the governor of Kaduna, a member of the APC, threatened to send people from "global institutions" home in body bags if they try to intervene in the election process.<sup>9</sup>

### **Ramifications**

The Nigerian election will likely be hotly contested, and with tempers already running high it is doubtful that any outcome will be accepted peacefully. At this time, it is unclear who is favored to win the election as we have been unable to find an election poll. No matter the result, both sides are already prepared to accuse the other of foul play. The rise in rhetoric between the two sides increases the odds of unrest. In the event that there is violence, we expect oil prices to rise slightly, although the magnitude of the increase will be limited by current excess capacity in the oil markets.

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<sup>8</sup><https://www.nytimes.com/2019/01/07/world/africa/nigeria-military-daily-trust-boko-haram.html>

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<sup>9</sup> <https://www.vanguardngr.com/2019/02/pdp-threatens-to-pull-out-of-peace-accord/>

*This report was prepared by Thomas Wash of Confluence Investment Management LLC and reflects the current opinion of the author. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.*

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