

Lagos State Government of Nigeria

2021 Final Municipal Rating Report



Lagos State Government of Nigeria

Rating Assigned:

A+

This is a municipal with good financial condition and strong capacity to meet local currency obligations in a timely manner

Outlook: Stable

Issue Date: 1 October 2021

Expiry Date: 30 September 2022

Previous Rating: A+

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RATING RATIONALE

- Agusto & Co. hereby affirms the “A+” rating assigned to the Lagos State Government (“Lagos”, “the State” or “LASG”) on account of the State’s resilient financial condition and strong capacity to meet local currency obligations in a timely manner from its internally generated revenue (IGR) and share of centrally collected revenue. Despite the adverse impact of the Covid-19 pandemic which culminated into a recession in Nigeria, the State’s topline performance remained resilient as total revenue (including grants and donations related to the Covid-19 pandemic) rose marginally by 2% to ₦658.5 billion in 2020 with further signs of growth in 2021. Although the civil unrest “EndSARS” which occurred in October 2020 resulted in the destruction of properties and loss of lives in various parts of Nigeria and Lagos in particular, we note that the State has made strategic investments in security and general infrastructure facelift to restore public confidence and favourable operating environment for businesses and households. Consequently, we retain our opinion that Lagos State remains one of the most strategic and economically viable states in the country that can function independently of the share of centrally distributed funds.
- In the financial year ended 31 December 2020 (FYE 2020), Lagos State recorded total revenue (including grants¹) of ₦658.5 billion, marginally higher by 2% than the prior year, while total expenditure² rose to ₦811 billion (2019: ₦577.8 billion), resulting in a deficit of ₦152.5 billion. In the same period, LASG’s posted a positive net operating cash flow (OCF) of ₦269.5 billion (2019: ₦241.4 billion) and an overall net cash position of ₦43.4 billion. As at FYE 2020, Lagos State’s total identifiable assets and liabilities stood at ₦2.56 trillion (2019: ₦2.4 trillion) and ₦1.07 trillion (2019: ₦957.5 billion) respectively.
- In 2020, Lagos State’s internally generated revenue (IGR) buoyed by Pay-As-You-Earn tax (PAYE), rose by 9% year-on-year to ₦451.9 billion (accounting for 71% of total revenue). In the same period, the State’s share of statutory allocation (SA) which dipped by 12% year-on-year to ₦51.3 billion due to decline in crude oil prices represented 8%, while the share of value added tax (rose by 23% year-on-year to ₦131.9 billion due to implementation of the new 7.5% VAT regime) accounted for 21% of revenue. Overall, Agusto & Co. notes positively the elasticity in Lagos State’s

¹This relates to one-off Covid-19 pandemic grants and donations amounting to ₦23.2 billion. If we adjust for the one-off grants, LASG’s total revenue in 2020 would have declined by just 1% to ₦635.2 billion, which typifies the resilient revenue profile of the State.

²This includes a net loss on foreign exchange due to currency devaluation on translation of year-end balances amounting to ₦120 billion. If we adjust for the net loss on FX, LASG’s total expenditure will amount to ₦691 billion, resulting in a deficit of ₦32.5 billion.

revenue profile and expects further improvement in the near term premised on the continued reopening of the global economy, increased commercial activities in the State as well as the ongoing Covid-19 vaccination roll-out success.

- As at 31 December 2020, Lagos State's total borrowings of ₦1.01 trillion represented 153% of 2019 revenue. Furthermore, LASG's net debt as a percentage of free cash flow of 247% and interest payment as a percentage of revenue which marginally declined to 10% in 2020 on account of the gains from the commercial debt restructuring in the year, are both in line with our expectations and better than many states in the country.
- Subsequent to the 2020 year-end, Lagos State exercised the early redemption option to repay the following bonds - ₦47 billion 16.5% 7-Year due 2023 (Series I), ₦46.3 billion 7-Year 16.75% due 2024 (Series II Tranche I) and ₦6.91 billion 6⁷/₁₂-Year 15.6% due 2024 (Series II Tranche III). In addition, the State obtained a Bridge facility from a consortium of banks which it utilized to redeem the aforementioned bonds due to the prevailing low interest rate environment. Going forward, Lagos State plans to access low-cost funds from the debt capital market through a bond issuance of ₦125 billion to refinance the Bridge facility and fund the construction, rehabilitation and upgrade of selected roads in the State.
- In the six months ended 30 June 2021, Lagos State reported total revenue (including grants) of ₦360.5 billion and we forecast total revenue to close at about ₦706 billion by the end of 2021 (representing an 11% growth from the prior year), with IGR accounting for 74%, while VAT and SA receipts will represent 20% and 6% respectively. In our opinion, Lagos State's revenue profile is stable and sustainable.
- The Year 2021 Budget of ₦1.163 trillion tagged "Budget of Rekindled Hope" split into capital expenditure (60%) and recurrent expenditure (40%), is meant to further advance the THEMES³ agenda across all areas with particular emphasis on youth employment by focusing on sectors with huge job-creating potential such as agriculture, construction, technology and security. In line with the historical trend, the State's 2021 Budget is expected to be funded largely with projected revenue of ₦971 billion (with IGR component of ₦723.8 billion) and the balance to be financed through a combination of external debts, domestic commercial borrowings and bond issuances.
- Going forward, the State Government remains committed to fostering a conducive environment where businesses and households would thrive by creating an enabling atmosphere. Thus, the State has prioritized development initiatives under the THEMES which cuts across critical sectors such as security, infrastructure, transportation, commerce and technology. Agusto & Co. believes that the successful execution of projects earmarked under this programme will result in an improved economic condition of Lagos State as we believe that it has the potential and the framework to ramp up IGR in the medium term.
- Based on the aforementioned, we hereby attach a **stable** outlook to the Lagos State Government of Nigeria.

³ THEMES - Traffic Management & Transportation, Health & Environment, Education & Technology, Making Lagos a 21st century Economy, Entertainment & Tourism and Security & Governance

Figure 1: Strengths, Weakness, Opportunities & Challenges

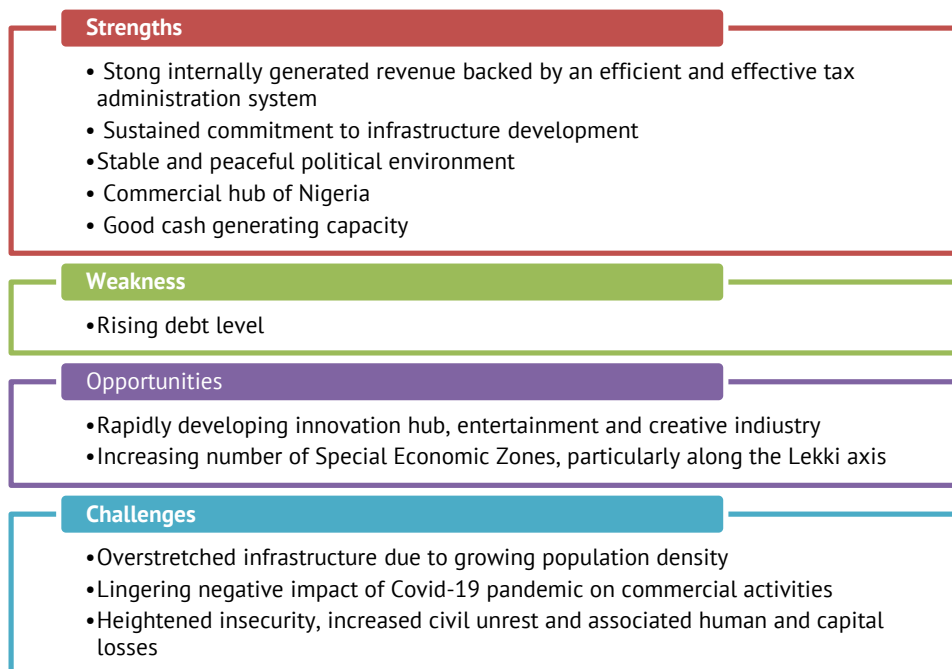
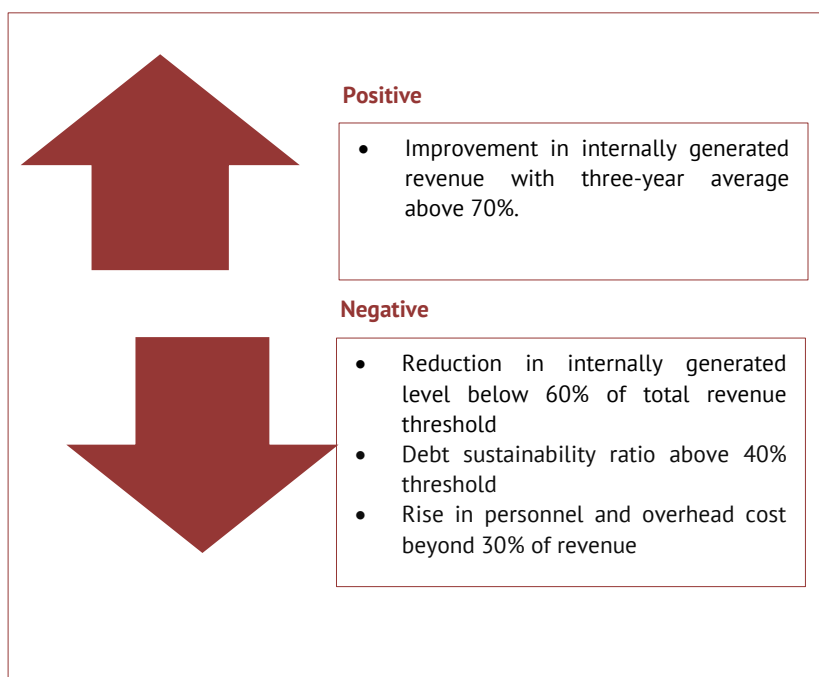


Figure 2: Rating Triggers



MUNICIPAL PROFILE

ABOUT LAGOS STATE

Lagos State was created on 27 May 1967 through the States Creation and Transitional Provisions Decree No. 14 of 1967, which divided Nigeria's Federation into 12 states. The State was Nigeria's administrative capital from 11 April 1968 until 12 December 1991, when the seat of Government was moved to Abuja.

Figure 3: Map of Lagos State



Lagos State is the smallest state in the country by landmass occupying 3,577 sq. km. The State is bounded in the North and East by Ogun State, in the West by the Republic of Benin and stretches over 180 kilometres along the Guinea Coast of the Bight of Benin on the Atlantic Ocean. Lagos consists of several landmasses separated by creeks, lagoons and rivers. The dominant language spoken in the State is Yoruba. Pidgin English (a diluted form of English) is also spoken by the majority of its residents.

The State comprises five administrative divisions – Ikorodu, Badagry, Ikeja, Lagos Island and Epe (IBILE), 20 Local Governments and 37 Local Council Development Areas. The Lagos Bureau of Statistics estimated the population of the State at 25.6 million people in 2018 with a population density of 892,990.6/ sq.km. The most populous local governments are Alimosho, Ajeromi/Ifelodun and Shomolu, while the State is also experiencing high population growth in Ibeju-Lekki and Epe local governments due to the ongoing land reclamation projects and an increasing number of residential dwellers. According to the National Bureau of Statistics Q4'2020 Unemployment Report, Lagos has the largest active labour force of 4.9 million in the country and has an unemployment rate of 37.14% and an underemployment rate of 4.52%.

ECONOMIC PROFILE

Lagos State is the commercial capital of Nigeria as it contributes a significant part to the Nation's Gross Domestic Product (GDP) and accounts for over 60% of Nigeria's industrial investments, foreign trade and commercial activities. In 2020, Lagos' GDP was estimated at ₦29.7 trillion⁴ and GDP per capita at \$2,831.2, with projected growth of 3% by end of 2021. The State has two airports (international and domestic, both located at Ikeja) and plays host to Nigeria's leading port, which is one of the largest and busiest in Africa (divided into three sections - the Lagos port, Apapa port & Tin Can port, each serving varying needs).

Under the current administration, the State has prioritized economic growth and development under the policy trust programme of "THEMES" which aims to make Lagos, Africa's model megacity and economic & financial hub. The THEMES programme which is being implemented over the four-year tenor of the Governor, Mr Babajide Sanwo-Olu, covers the following areas: Traffic Management & Transportation, Health & Environment, Education & Technology, Making Lagos a 21st century Economy, Entertainment & Tourism and Security & Governance.

⁴ Lagos Bureau of Statistics, Ministry of Economic Planning and Budget - Lagos State Government

POLITICAL STRUCTURE

There are three arms of government in Lagos State, namely the Executive, the Legislative and the Judiciary. Each arm is empowered by the 1999 Constitution of the Federal Republic of Nigeria to function independently and in a collaborative manner for the overall development of the State and the welfare of the citizens.

The Executive arm of the State Government is responsible for daily administration and is led by the Executive Governor, **Mr Babajide Olusola Sanwo-Olu**, who is assisted by the Deputy Governor – **Dr Kadri Obafemi Hamzat** and the State Executive Council.

The Legislative arm of the State Government is empowered by Section 90 of the 1999 Constitution of the Federal Republic of Nigeria as amended to legislate for Lagos State. The Speaker, **Rt. Hon. Mudashiru Ajayi Obasa** leads the Lagos State House of Assembly. All the 40 elected members of the State House of Assembly belong to the All Progressive Congress (APC) political party.

The Judicial arm of government is also authorized by the 1999 Constitution and laws of the State with the responsibility for the general administration of justice in the State. The Lagos State judiciary is made up of the State High Courts, Magistrate Courts and Customary Courts. The High Court system in the State comprises the Criminal Division, the Lands Division, the Family and Probate Division, the Commercial (Fast Track) Division, the General Civil Division, the Special Offences Courts and the Sexual Offences Courts. The High Court of Lagos is the highest court of law in the State and **Hon. Justice Kazeem Olanrewaju Alogba** is the Chief Judge.

Profile of LASG Executive Council Members:

The Governor, Mr Babajide Sanwo-Olu holds a Bachelor's degree in Surveying & Geo-Informatics and a Master of Business Administration (MBA) in Management, both from the University of Lagos. Mr Sanwo-Olu is also an alumnus of the Harvard Kennedy School of Government, London Business School and the Lagos Business School. In addition, he is a member of the Nigerian Institute of Directors (IOD), Chartered Institute of Personnel Management (CIPM), and Fellow of Nigeria Institute of Training and Development (NITAD).

In 2003, he was appointed first as Special Adviser to the Deputy Governor on Corporate Matters; and as Special Adviser to the Executive Governor on Corporate Matters in 2004. Later, he was appointed acting Commissioner for Economic Planning & Budget from 2004 to 2005 and became the substantive Commissioner for Commerce and Industry in 2007. Mr Sanwo-Olu was appointed the Chief Executive Officer of the Lagos State Property Development Corporation (LSPDC) in 2016. On 29 May 2019, he was sworn in as the elected Governor of Lagos State under the APC political party for a term of four years.

The Deputy Governor, Dr Kadri Obafemi Hamzat holds a Bachelor's degree in Agricultural Engineering and a Master's degree in Agricultural Engineering, both from the University of Ibadan. Dr Hamzat obtained a PhD in System Process Engineering from Cranfield University, England and is also an alumnus of the Harvard Kennedy School Executive Education Programme. His prior work experience before joining politics in 2005 covers roles at RTP Consulting Services, City of New York, Columbia University, Merrill Lynch Inc, Morgan Stanley and as Chief Information Officer (CIO) and Group Head, IT Strategy of Oando Plc, Lagos.

In 2005, he was appointed as Commissioner for Science and Technology and continued in that position until 2011, when he was appointed as Commissioner for Works and Infrastructure; a position he held till May 2015. In January 2016, Dr Hamzat was appointed as Special Adviser Technical to the Minister for Power, Works and Housing – Mr Babatunde Raji Fashola and continued in that position until August 2018. In October 2018, he

teamed up with Mr Babajide Sanwo-Olu, to run under the All Progressive Congress (APC) political party and was sworn in as Deputy Governor on 29 May 2019 for a term of four years.

Table 1: Members of the Executive Council of Lagos State Government

Executive Council Members	Responsibility/Portfolio
Mrs Folashade Sherifat Jaji	Secretary to State Government
Mr Hakeem Muri-Okunola	Head of Service
Mr Tayo-Akinmade Ayinde	Chief of Staff
Mr Gboyega Soyannwo	Deputy Chief of Staff
Ms Ruth Abisola Olusanya	Commissioner, Agriculture
Dr (Mrs) Lola Akande	Commissioner, Commerce, Industry and Cooperatives
Mr Samuel Egube	Commissioner, Economic Planning & Budget
Mrs Folashade Adefisayo	Commissioner, Education
Mr Olalere Odusote	Commissioner, Energy and Mineral Resources
Mr Tunji Bello	Commissioner, Environment and Water Resources
Mrs Ajibola Ponle	Commissioner, Establishment, Training and Pensions
Dr Rabiun Onaolapo Olowo	Commissioner, Finance
Prof Akinola Abayomi	Commissioner, Health
Prince Anofiu Olanrewaju Elegushi	Commissioner, Home Affairs
Mr Moruf Akinderu Fatai	Commissioner, Housing
Mr Gbenga Omotosho	Commissioner, Information and Strategy
Mr Moyosore Onigbanjo (SAN)	Commissioner, Justice / Attorney General
Dr Wale Ahmed	Commissioner, Local Government and Community Affairs
Dr Idris Salako	Commissioner, Physical Planning and Urban Development
Mr Hakeem Fahm	Commissioner, Science and Technology
Engr Tayo Bamgbose-Martins	Commissioner, Special Duties & Inter-Governmental Relation
Phar (Mrs) Uzamat Akinbile-Yusuf	Commissioner, Tourism, Arts & Culture
Dr Frederic Oladeinde	Commissioner, Transportation
Arch Kabiru Ahmed Abdullahi	Commissioner, Waterfront Infrastructure Development
Mrs Yetunde Arobieke	Commissioner, Wealth Creation and Employment
Mrs Cecilia Bolaji Dada	Commissioner, Women Affairs and Poverty Alleviation
Mr Ganiyu Olusegun Dawodu	Commissioner, Youth and Social Development
Mr Solomon Saanu Bonu	Special Adviser, Arts & Culture
Mr Oyerinde Olugbenga Olanrewaju	Special Adviser, Central Business District
Princess Aderemi Adebawale	Special Adviser, Civic Engagement
Mr Oladele Ajayi	Special Adviser, Commerce and Industry
Mr Joe Igboke	Special Adviser, Drainage Services
Mr Tokunbo Wahab	Special Adviser, Education
Mrs Adetoke Benson-Awoyinka	Special Adviser, Housing
Mr Olatubosun Alake	Special Adviser, Innovation and Technology
Mr Afolabi Ayantayo	Special Adviser, Parastatals Monitoring Office
Mrs Solape Hammond	Special Adviser, Sustainable Development Goals and Lagos Global
Mr Oluwatoyin Fayinka	Special Adviser, Transportation
Hon Ayuba Ganiu Adele	Special Adviser, Urban Development
Engr Aramide Adeyoye	Special Adviser, Works & Infrastructure

FINANCIAL CONDITION

ANALYSTS' COMMENTS

- Lagos State Government has prepared its Financial Statements for the year ended 31 December 2020 (the fifth in the series) in line with the International Public Sector Accounting Standards (IPSASs) Accrual Based Accounting.

FINANCIAL PERFORMANCE

REVENUE PROFILE

Lagos State's primary sources of internally generated revenue include taxes on personal income, fines, licenses, fees and levies on business activities, as well as income from investments. Also, the State receives a monthly share of income from the Federation Account and Value Added Tax Pool as well as grants from development institutions for specific projects.

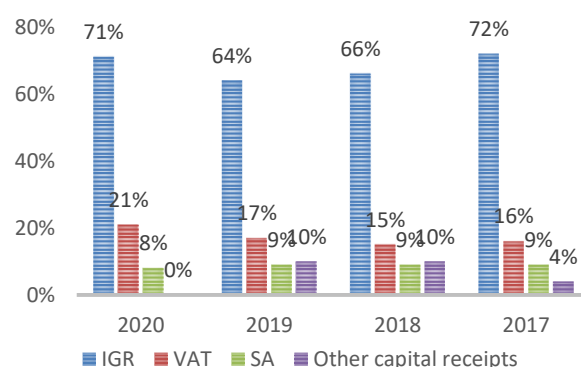
The year 2020 was beset with several challenges globally and locally, which impacted the State's economic profile as well as its overall financial condition. Firstly, the State is the epicentre of Covid-19 cases in the country, which prompted a complete and later partial lockdown of commercial activities for several weeks in the year. Also, the civil unrest "EndSARS" which culminated in the wanton destruction of properties and loss of lives (with Lagos as a hotspot) further impacted the State's fragile recovery from the pandemic in October 2020. These twin events placed a huge recovery burden on the State in terms of infrastructural facilities and restoring public confidence and simultaneously impacted the State's overall financial performance when compared to the 2020 budget as well as the revised 2020 Covid-19 budget.

Notwithstanding the aforementioned challenges, Lagos State remained resilient and reported total revenue of ₦658.5 billion, which was 2% higher than the prior year. The marginal increase in revenue was mainly due to the rise in one-off grants and donations of ₦23.2 billion related to the Covid-19 pandemic. If we adjust for the one-off grants, LASG's total revenue in 2020 would have declined by just 1% year-on-year to ₦635.2 billion, which typifies the resilient and robust revenue profile of the State.

A breakdown of Lagos State's total revenue⁵ for FYE 2020 showed that income from internally generated revenue (which increased by 9% year-on-year to ₦451.9 billion) accounted for 71% (2019: 64%), while statutory allocation centrally distributed by the Federal Government (dropped by 12% year-on-year to ₦51.3 billion) represented 8% and share of value added tax (which rose by 23% year-on-year to ₦131.9 billion) accounted for 21% of revenue. In addition, due to paucity of funds, the State did not record any capital inflows from the FGN relating to refund on road construction in 2020, compared to the prior year when ₦63.6 billion was received (representing 10% of revenue).

We recognize positively that Lagos State's Pay-As-You-Earn tax (PAYE), which is considered the most stable and sustainable source of revenue for state governments in Nigeria, grew by 5% y-o-y to account for 65% of IGR in 2020. This is a further testament to the State's robust and institutionalized revenue collection framework which ensured that personal income taxes were collected during the Covid-19 induced lockdown. Furthermore, we note that income from other taxes⁶, levies, fines & fees⁷, investment income⁸ and asset sales⁹ all increased

Figure 4: Revenue Breakdown (2017 - 2020)



⁵ This excludes the one-off grants and donations

⁶ The taxes include direct assessment, capital gain tax, entertainment tax, withholding tax, tax penalties, property tax, stamp duties, development levy, business premises, tax on contract and other tax receipts

year-on-year to represent 15%, 17%, 1% and 3% respectively of IGR in the period. In our view, the effective and efficient tax administration and collection system in the State coupled with the deployment of e-revenue collection systems is the bedrock of LASG's stable and sustainable IGR profile.

Premised on the implementation of the new VAT regime which increased by 50% from 1 February 2020 to 7.5%, LASG reported higher VAT receipts of ₦131.9 billion in 2020 (2019: ₦107.7 billion) and we expect this improvement to continue due to increased commercial activities in the State. This is also further supported by the FGN's revolutionized value-added tax administration system which encourages the online filing of tax returns, automation of collection and remittance of VAT as well as compliance-based system.

In 2020, the State's share of statutory allocation declined by 12% to ₦51.3 billion as crude oil prices plunged to an average of \$39.9 per barrel in H1'2020¹⁰ (though gradually improved in H2'2020) amidst reduction in crude oil consumption as well as supply chain constraints globally associated with the negative impact of the Covid-19 pandemic. However, the cushioning impact on FGN's centrally collected revenue (distributed to the three tiers of government) in 2020 was the stable crude oil production volumes coupled with a higher exchange rate for converting crude oil receipts¹¹ thus moderating the negative impact of fluctuations in crude oil prices in the international market in H1'2020. With the uptick in crude oil prices since H2'2020 premised on growing crude oil demand following the curbing of the Covid-19 pandemic through ongoing vaccination as well as stable local crude oil production volumes, we expect the State's share of statutory allocation to etch higher in 2021 to about ₦55 billion.

Overall, Agusto & Co. recognizes the elasticity in the State's revenue profile in FYE 2020 and H1'2021 and expects further improvement in the near term premised on increased commercial activities in the State as well as the ongoing Covid-19 vaccination roll-out success. On the back of this, we forecast Lagos State's total revenue to rise by 11% to about ₦706 billion by the end of 2021, with IGR accounting for 74%, while VAT and statutory allocation will represent 20% and 6% respectively. In our opinion, Lagos State remains one of the most economically viable states in the country and its revenue profile is resilient and sustainable.

CASH FLOW PROFILE

In the financial year ended 31 December 2020, Lagos State Government reported a total inflow of cash from operating activities of ₦656.1 billion (2019: ₦644.2 billion) and outflow of cash for operating activities of ₦386.5 billion (2019: ₦402.8 billion), resulting in net operating cash flow (OCF) of ₦269.5 billion (2019: ₦241.3 billion). Furthermore, LASG reported a negative net cash flow from investing activities of ₦312.3 billion and positive net cash flow from financing activities of ₦86.2 billion on account of increased borrowings in the period, resulting in an overall positive net cash position of ₦43.4 billion in FYE 2020.

In 2020, the State's discretionary cash flow (total revenue less mandatory payments¹²) to revenue ratio of 59% (2019: 66%) was in line with our expectation and compares better to Ogun (55%), Enugu (45%) and Katsina (37%). Furthermore, LASG's net debt as a percentage of free cash flow¹³ of 247% (2019: 177%) is within our benchmark. In our opinion, Lagos State has a good and sustainable cash-generating capacity bolstered by its strong internally generated revenue.

⁷ This relates to fines and fees, licenses and land use charge (LUC) – this significantly dipped by 82% from the prior year due to the proposed changes to the LUC rates which met strong resistance and non-compliance by affected property owners

⁸ This represents dividend income on State Owned Enterprises, interest income on short term deposits and income from investments

⁹ This includes income from land sales & regularization, sale of vehicle number plate, sale of housing units, survey fees, etc.

¹⁰ The average crude oil prices in H1'2019 was \$67.7 per barrel.

¹¹ A two-step currency devaluation occurred in April and July 2020 pegging the official exchange rate at ₦381/\$ from previously ₦306/\$

¹² This refers to personnel expenses, public debt charges (interest payments) and transfers and subvention to parastatals

¹³ This is also known as discretionary cash flow

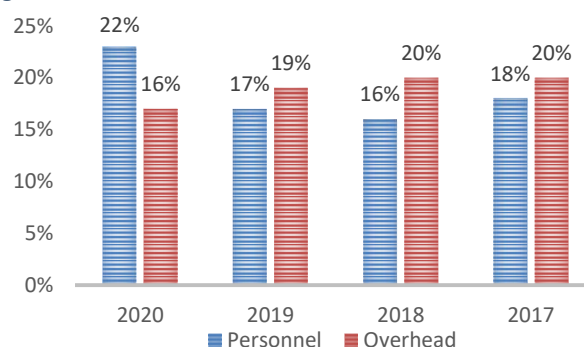
EXPENDITURE PROFILE

In the financial year ended 31 December 2020, Lagos State recorded total expenses of ₦811 billion (2019: ₦577.8 billion) mainly due to higher capital expenditure and significant rise in net loss on foreign exchange transactions as a result of translation of year-end foreign currency debt balances elicited by currency devaluation. Thus, the State reported an overall deficit (total revenue less expenditure) of ₦152.5 billion, down from a surplus of ₦66.9 billion in the prior year. However, if we adjust the net loss on foreign exchange transactions of ₦120 billion, LASG would have reported total expenses of ₦691 billion and a deficit of ₦32.5 billion for FYE 2020. The State's total expenditure in 2020 was split into operating expenses (38%) and non-operating expenses (62%) in line with the IPSAS framework to reflect all expenses whether paid for or not. Operating expenses include salaries, wages & employee benefits, transfers & subventions to parastatals and general administrative expenses, while non-operating expenses consist of capital expenditure, public debt charges, and depreciation on non-current assets and net loss on foreign exchange transactions.

In FYE 2020, Lagos State's total operating expenses rose by 11% to ₦309.8 billion with personnel cost¹⁴ accounting for 47%, while general and administrative expenses (i.e. overheads¹⁵) represented 35% and subvention to parastatals 18%. Premised on the full implementation of the minimum wage, increase in salaries prior to the pandemic and the State's desire not to lay-off any employee during the Covid-19 induced lockdown, LASG's personnel expenses rose by 37% in absolute terms y-o-y to ₦146.3 billion, representing 22% of revenue (2019: 17%), which we consider to be satisfactory. In contrast, the State's overhead costs declined in absolute terms by 11% and represented 16% of revenue, which we consider to be in line with our benchmark. We note positively that Lagos State's personnel and overhead costs as a percentage of revenue in FYE 2020 are lower than many states in the country - Ogun (26% & 11%), Enugu (39% & 33%) and Katsina (35% & 25%).

In the year ended 31 December 2020, Lagos State's non-operating expenses consisting of capital expenditure (40%), net loss on foreign exchange transactions (24%), depreciation on property, plant and equipment (23%), public debt charges (12%) and damaged assets¹⁶ (1%) increased markedly to ₦501.2 billion (2019: ₦299.2 billion) mainly due to higher capital spending on construction and rehabilitation of roads, drainages and bridges as well as non-cash foreign exchange loss owing to currency devaluation.

Figure 5: Personnel & Overhead Costs to Revenue (2017 - 2020)



We note that Lagos State spent ₦201.7 billion representing 31% of revenue in 2020, mainly on infrastructural facilities as well as construction and rehabilitation of roads, drainages and bridges to improve the operating environment.

Going forward, we expect capital expenditure to rise in a bid to further improve the overall socio-economic condition of the State and also to replace damaged properties during the civil unrest in October 2020. However, we estimate personnel and overhead costs to revenue ratios to flatten at about 22% and 20% respectively by the end of 2021 in line with the 5-year (2016 – 2020) average trend.

In our view, the State's overall expenditure profile is satisfactory.

¹⁴ This comprises wages, salaries and employment benefits of civil servants and public office holders in the State

¹⁵ This consist of general and administrative expenses such as consultancy & professional services, general office expenses, special duties expenses, security expenses maintenance services and other parastatals overheads

¹⁶ The refers to the value of the assets of the State Government destroyed during the nationwide "EndSARS" protest in October 2020. The identified assets include 49 burnt buses, JIC Taylor Court House, Magistrate Court Igboosere and various traffic signal lights

FINANCIAL POSITION

ASSET & LIABILITY STRUCTURE

The International Public Sector Accounting Standards (IPSAS) allows for a three-year transitional period for recognition and measurement of assets and liabilities in line with IPSAS 33. Although Lagos State elected to adopt the transitional exemptions in IPSAS 33, the State had complied with the extant guidelines and provisions stipulated by IPSASs except for the full consolidation of subsidiaries, associates and joint ventures, hence LASG is unable to make an explicit statement of its full compliance with the accrual-based IPSAS as at 31 December 2020.

As at FYE 2020, Lagos State's total identified assets stood at ₦2.56 trillion (2019: ₦2.4 trillion) split into non-current assets (95%) and current assets (5%). The State's portfolio of recognized non-current assets in line with IPSAS comprised property, plant and equipment¹⁷ (97%), available-for-sale-investments¹⁸ (2%) and other financial assets (1%). In line with the IPSAS framework, Lagos State continues to use the cost model¹⁹ to measure its non-current and current assets with a view to full compliance in the medium term.

Lagos State's total identifiable liabilities stood at ₦1.07 trillion as at 31 December 2020, up by 12% from the prior year mainly due to an increase in commercial borrowings in the year under review. Further analysis revealed that total borrowings (comprising internal, external debts and bonds in issue) accounted for 94% of Lagos State's total liabilities as at FYE 2020, while payables and other liabilities, retirement benefit obligations and finance lease obligations²⁰ represented 4%, 1% and 1% respectively. As at the same date, the State's total debt of ₦1.01 trillion (2019: ₦785.8 billion) consisted of foreign borrowing (54%) and domestic debt 46% (split into local bonds in issue 24% and internal commercial bank facilities 22%).

As at FYE 2020, Lagos State's external debt portfolio comprised 25 facilities for various projects with different international institutions repayable in foreign currencies with an outstanding principal value of \$1.43 billion (equivalent to ₦543.1 billion), with tenor between 20 and 40 years, moratorium periods of 5 and 13 years and concessionary interest rates between 0.75% and 2.37% per annum. All the foreign debts are backed by irrevocable standing payment orders (ISPO) which serve as security for the facilities and outstanding balances are translated using the prevailing exchange rate at the reporting date. Agusto & Co. notes positively that the concessionary rates coupled with the longer tenors, reduces Lagos' annual debt service burden, except for intermittent depreciation of the local currency as these borrowings were not hedged.

As at 31 December 2020, Lagos State had 24 facilities with different local commercial banks, following repayment of 11 during the year, with a cumulative outstanding principal value of ₦226.7 billion at an interest rate of 10% to 12% per annum and average unexpired tenor above 36 months. Agusto & Co. recognizes the finance cost savings initiatives embarked upon over the last two years through restructuring of local borrowings to reduce the overall debt service burden of the State.

¹⁷ This refers to property plant and equipment such as infrastructure assets, land and buildings, plant and machinery, office equipment, furniture and fittings, computer equipment, motor vehicles and capital work in progress

¹⁸ This represents LASG's investment in Quoted Securities (Julius Berger Nigeria Plc and Lasaco Assurance Plc) and Unquoted Investments in various companies as at 31 December 2020

¹⁹ Under the cost model, annual depreciation charges using applicable rates will apply to relevant asset classes on a periodic basis

²⁰ This refers to lease agreements with five independent power generation companies in the State (Akute Power Limited, Island Power Limited, Alausa Power Limited, Mainland Power Limited and PIPP LVI Genco Limited) with a minimum lease term of ten years each. The lease agreements state that the power generation companies are to build and operate power plants which would provide electricity to LASG, with a minimum 97% guaranteed availability, thus they have been treated as finance lease in line with relevant IPSASs.

As at 31 December 2020, Lagos State had three bonds in issue (following the redemption of the former ₦87.5 billion 7-Year 13.5% Fixed Rate Bond in November 2020) with a cumulative outstanding principal balance of ₦237.7 billion split as follows:

- ₦47 billion 16.5% 7-Year due 2023.
- ₦97.3 billion Series II Bond (made up of ₦46.3 billion 7-Year 16.75% due 2024- Tranche I, ₦38.7 billion 10-Year 17.25% due 2027-Tranche II, ₦6.91 billion 6⁷/₁₂-Year 15.6% due 2024- Tranche III and ₦5.34 billion 9⁷/₁₂-Year 15.85% due 2027- Tranche IV).
- ₦100 billion 10-Year 12.25% Fixed Rate Bond Due 2030.

All LASG bonds in issue are backed by monthly ISPO deductions on the State's share of statutory allocation and internally generated revenue. Also, the total cumulative amount in the sinking fund account of the respective bonds stood at ₦23 billion as at FYE 2020.

LASG's net debt as a percentage of free cash flow of 247% and interest payment as a percentage of revenue which marginally declined to 10% in 2020 on account of the gains from the debt restructuring activities in the year, were both in line with our expectations and considered satisfactory.

Subsequent to FYE 2020, Lagos State exercised the early redemption option to repay the following bonds - ₦47 billion 16.5% 7-Year due 2023, ₦46.3 billion 7-Year 16.75% due 2024 (Series II Tranche I) and ₦6.91 billion 6⁷/₁₂-Year 15.6% due 2024 (Series II Tranche III). In addition, the State obtained a Bridge-To-Bond facility of ₦82 billion from a consortium of banks which it utilized to redeem the aforementioned bonds. Going forward, Lagos State plans to access low-cost funds from the debt capital market in line with the State's approved financing plan of ₦125 billion to refinance the Bridge-To-Bond facility and fund the construction, rehabilitation and upgrade of selected roads in the State.

We expect Lagos State to continue to service the financial obligations principally supported by its good internally generated revenue, strong track record and good credit history which it leverages to obtain financing at competitive rates and at short notices.

OUTLOOK

The year 2020 was plagued by several challenges which impacted Lagos State's economic profile and overall financial condition. Firstly, the State was the hub for COVID-19 cases in the country, thus resulting in a complete and later partial lockdown of business activities especially in the second and third quarters of 2020. Furthermore, the "EndSARS" civil unrest in October 2020 (with Lagos as hotbed) culminated into the wanton destruction of properties and loss of lives. Agosto & Co. notes that the knock-on effect of these twin events coupled with the dwindling revenue of the FGN shared to the three tiers of government impacted the State's financial condition in 2020. Nevertheless, the phased-reopening of global economies, increased commercial activities in the State as well as the ongoing Covid-19 vaccination roll-out success in the first half of 2021 are cursors of an improved operating environment and we expect this to continue in the near term supported by the harmonious working relationship amongst the tiers of government in the State.

In the first half of 2021, the State exercised its early redemption option to repay three existing bonds in issue with a Bridge Facility provided by a consortium of banks. Going forward, Lagos State plans to access funds (at a cheaper rate given the prevailing low-interest-rate environment) from the debt capital market in the sum of ₦125 billion to refinance the Bridge facility and fund the construction, rehabilitation and upgrade of selected roads in the State. Agosto & Co. notes that the aforementioned initiatives if successful will reduce the cash flow burden on Lagos State in the short to medium term and improve the welfare of the citizens.

A review of the Lagos State's 2021 Budget of ₦1.163 trillion tagged "*Budget of Rekindled Hope*" for the period ended 30 June 2021 revealed an average overall revenue performance of 37.7% of the budget compared with the 50% projection as at H1'2021, with receipts from FAAC allocation outperforming at 52.3%, PAYE tax receipts at 44.7%, non-tax income and grants at 21.5% and 17.4% of budget respectively. LASG's recurrent expenditure performance compared to the budget was at 45.2% as at end of June 2021, while capital expenditure performance closed lower at 38.8%. Going forward, the State plans to ramp up its budget performance before the end of 2021 by deepening non-tax revenue collections, reducing leakages and optimising procurement of consumables to keep recurrent performance within budget. To actualise the capital expenditure budget performance by end of 2021, the State plans to utilise the proceeds of the Series IV bond issuance (after refinancing the Bridge-To-Bond Facility) to fund the rehabilitation of selected roads across the State.

Overall, we do not envisage a significant decline in Lagos State's ability to generate IGR or receipt of its share of centrally collected revenue from the Federal Government in the short to medium term, which will impair the State's capacity to meet its local currency obligations as and when due. In our view, Lagos State should be able to (a large extent more than most states in the country) withstand any negative macroeconomic headwinds due to its strong internally generated revenue and good economic profile. We have therefore attached a **stable** outlook to the Lagos State Government of Nigeria.

FINANCIAL SUMMARY

REVENUE & SPENDING	IPSAS 2020		IPSAS 2019		IPSAS 2018		IPSAS 2017	
	₦'mns	%	₦'mns	%	₦'mns	%	₦'mns	%
REVENUE								
Tax revenue								
Personal Income Tax	292,479.9	46%	279,792.3	43%	250,011.7	38%	234,089.0	46%
Share of VAT collected centrally	131,970.2	21%	107,704.2	17%	99,055.2	15%	80,231.7	16%
Share of other revenues collected centrally (Stat. Allocation)	51,348.4	8%	58,142.3	9%	59,743.1	9%	43,331.7	9%
Other capital receipts (refund from Paris Club and refund by FGN for Road Construction)	-		63,648.9	10%	64,275.2	10%	18,216.6	4%
Other taxes	66,582.4	10%	68,208.8	11%	65,046.6	10%	60,139.5	12%
	542,380.8	85%	577,496.5	90%	538,131.7	83%	436,008.5	86%
Non-tax revenue								
Asset sales	13,927.93	2%	8,972.28	1%	18,226.43	3%	10,020.35	2%
Investment income	3,540.5	1%	3,239.0	1%	4,624.2	1%	10,122.0	2%
Others - levies, fines & fees	75,416.9	12%	54,571.0	8%	91,134.4	14%	53,305.0	10%
	92,885.3	15%	66,782.3	10%	113,985.0	17%	73,447.3	14%
TOTAL REVENUE	635,266.1	100%	644,278.8	100%	652,116.7	100%	509,455.8	100%
<i>Of which internally generated revenue (IGR) is</i>	451,947.5	71%	414,783.4	64%	429,043.3	66%	367,675.9	72%
Grants	23,297.7	-	483.9	-	906.1	-	1,541.8	-
TOTAL REVENUE & GRANTS	658,563.7	-	644,762.7	-	653,022.9	-	510,997.6	-
SPENDING								
Transfers (including pension costs)	56,559.3	10%	50,825.2	11%	38,330.2	7%	38,189.7	7%
Interest payments	56,881.7	10%	62,533.2	13%	72,453.6	13%	65,613.2	11%
MDA spending	454,981.3	80%	362,247.8	76%	444,572.4	80%	474,651.4	82%
TOTAL SPENDING	568,422.3	100%	475,606.2	100%	555,356.3	100%	578,454.3	100%
<i>MDA spending is made up of</i>								
Personnel costs	146,383.0	26%	107,132.2	23%	101,901.1	18%	92,238.7	16%
Purchase of goods & services	106,880.8	19%	120,594.0	25%	132,715.7	24%	104,241.7	18%
Capital expenditure	201,717.5	35%	134,521.7	28%	209,955.6	38%	278,171.0	48%
TOTAL MDA SPENDING	454,981.3	80%	362,247.8	76%	444,572.4	80%	474,651.4	82%
BUDGET BALANCE	90,141.4		169,156.5		97,666.6		(67,456.7)	
BUDGET BALANCE AS % OF GDP	0.3%		0.5%		0.3%		-0.2%	
FINANCING								
Surplus of prior years	3,430.2		3,396.3		3,362.6		(196,759.1)	
Domestic borrowing (net)	93,195.2		(27,893.8)		(31,921.9)		15,937.0	
External borrowing (net)	(7,039.0)		(7,262.6)		(6,547.4)		6,696.8	
Other								
TOTAL FINANCING	89,586.4		(31,760.2)		(35,106.6)		(174,125.3)	
Foreign Debts- New Borrowings	10,692.2		1,543.9		-		13,840.0	
Repayment during the year	17,731.2		8,806.5		6,547.4		7,143.2	
Foreign Debt Balance	543,125.2		428,723.3		438,249.1		454,414.0	
Domestic- New Borrowings	225,296.7		116,090.3		45,000.0		137,387.0	
Repayment during the year	132,101.4		143,984.1		76,921.9		121,450.0	
Domestic Debt Balance	464,338.9		357,120.1		359,180.8		390,168.7	
Total Debt Balance	1,007,464.1		785,843.4		797,429.9		844,582.7	

KEY RATIOS	2020	2019	2018	2017
Revenue				
IGR as % of GDP	2%	1%	1%	1%
Tax revenue as % of GDP	2%	2%	2%	2%
Total revenue as % of GDP	2%	2%	2%	2%
IGR as % of total revenue & grants	69%	64%	66%	72%
Tax revenue as % of IGR	65%	67%	58%	64%
Growth in tax revenue	-6%	7%	23%	18%
Spending				
Spending as % of GDP	2%	1%	2%	2%
Non-discretionary spending* as % of tax revenue	48%	38%	40%	45%
Capital expenditure as % of total spending	35%	28%	38%	48%
Payroll as % of revenue	22%	17%	16%	18%
Other overheads as a % of revenue	16%	19%	20%	20%
Budget balance/revenue	14%	26%	15%	-13%
Leverage				
Budget balance (₦'mns)	90,141.44	169,156.51	97,666.57	(67,456.69)
Debt as % of nominal GDP	3%	3%	3%	3%
Interest payments as % of total revenue	9%	10%	11%	13%
Principal due as % of Revenue	23%	18%	18%	24%
Financial flexibility				
Discretionary revenue** as % of total revenue	59%	66%	67%	62%
Net Debt as % of Free cash flow***	247%	177%	159%	250%
Share of savings in "excess crude account" (₦'mns)				
Non-discretionary Spending as % of total spending	46%	46%	38%	34%
Outstanding Debt/Revenue	159%	122%	122%	166%
Discretionary cash flow divided by interest payment	6.60	6.78	6.07	4.78
* Non-discretionary spending is made up of statutory transfers, interest payments and personnel costs				
** Discretionary revenue is total revenue minus non-discretionary spending				
*** Free cash flow is defined as revenue minus non-discretionary spending				

RATING DEFINITIONS

Aaa	This is the highest rating category. It indicates a municipal with impeccable financial condition and overwhelming capacity to meet local currency obligations in a timely manner.
Aa	This is a municipal that possesses very strong financial condition and very strong capacity to meet to meet local currency obligations in a timely manner.
A	This is a municipal with good financial condition and strong capacity to meet local currency obligations in a timely manner.
Bbb	This refers to municipal with satisfactory financial condition and adequate capacity to meet local currency obligations in a timely manner.
Bb	This refers to municipal with satisfactory financial condition but ability to meet local currency obligations in a timely manner may be contingent upon refinancing.
B	This refers to a municipal that has weak financial condition and ability to meet local currency obligations in a timely manner is contingent on refinancing.
C	This refers to a municipal with very weak financial condition and cash flows to meet obligations are inadequate therefore likelihood of default is high.
D	Municipal In default.

Rating Category Modifiers

A "+" (plus) or "-" (minus) sign may be assigned to ratings from 'Aa' to 'C' to reflect comparative position within the rating category. Therefore, a rating with + (plus) attached to it is a notch higher than a rating without the + (plus) sign and two notches higher than a rating with the - (minus) sign.

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