

# FDC Economic Bulletin

September 16, 2016

## *Headline inflation rate surges to 17.6%*

Headline inflation (YoY) in Nigeria spiked to 17.6% in August, a 0.5% increase from that of July. This was as correctly forecast by the FDC Think tank. It is the seventh consecutive monthly increase in inflation and an 11-year high. The major source of pricing pressure is the non-food basket, a victim of supply shocks and forex scarcity. The tightening stance of the CBN has increased the marginal propensity to save and consumer resistance. The divergence between year on year inflation, which is rocketing, and the declining month on month inflation is becoming more stark.

**Chart 1: Rate of monthly change (%)**



Source : NBS, FDC Think Tank

Food inflation increased by 0.6% to 16.4% in August due to the pass through effect of a weaker naira. The scarcity of forex is propelling a new wave of smuggling of local staples like maize, sorghum and cassava to neighbouring countries. The highest contributors to the increase in the food basket were meat, fish, bread and cereals. Imported food inflation increased by 0.2% to 20.7% in August. Core inflation defined as inflation less seasonality increased by 0.3% to 17.2% in August, driven primarily by fuel, clothing, footwear, books and stationery. Education expenses increased also due to preparations for a new academic session. The urban areas witnessed less inflationary pressures as the index increased only by 0.4% to 19.3% in August, while the rural index increased by 0.6% to 16.1% in August.

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Imported inflation continues to be a key determinant to the increase in the rate of headline inflation. The naira depreciated by about 9.6% in the month of August at the parallel market to N425.

In spite of increased food supply due to the harvests, flooding has created logistics bottlenecks. The slowdown in core inflation, which increased by 0.3% in August is due to a marginal improvement in power supply. Power output from the national grid increased by 19.9% to 3,300 MW in August. Average diesel price across the country declined by 4.8% to N196.53 in August while premium motor spirit declined by 0.7% to N147. However, the year-on-year increase in energy prices is being reflected in headline inflation.

### **Monetary Policy Committee meeting – Committee under pressure**

The divergence between year on year headline inflation and the annualized monthly rate of 6.17% poses a major dilemma to the apex bank. Even though the monthly measure is more relevant to inflation expectations, it may need to maintain consistency with the previous measure.

The clamour for a stimulus package and lower interest rates by the government and public will force a more accommodative stance by the committee in spite of other considerations.

### **The Impact**

The high inflation environment has reduced consumer spending, real returns and corporate profitability margins. The markets have reacted accordingly.

### **Fixed Income and Money market**

In all, the CBN has mopped up N668.09bn this quarter. This is 3.08% of M2.



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## Stock market

The performance of the Nigerian bourse may be affected by the increasing inflation rate as a possible increase in fixed income rates could attract investors. The Nigeria ASI has declined by (3.2%) YTD. With cost of production increasing amidst forex challenges, earnings of listed companies may be significantly hit in Q3 and FY'16.

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