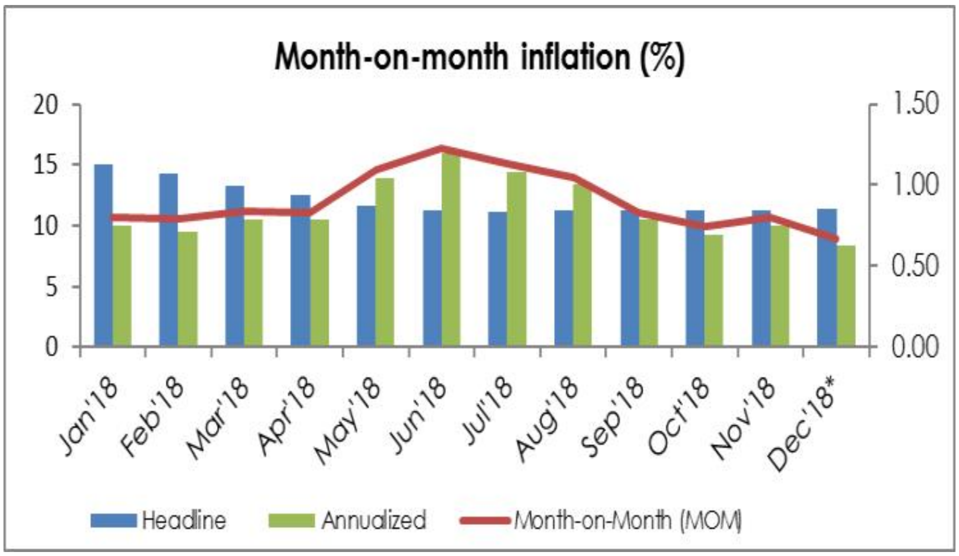
FDC Economic Bulletin

January 10, 2019

Annual headline inflation to increase but monthly price level down

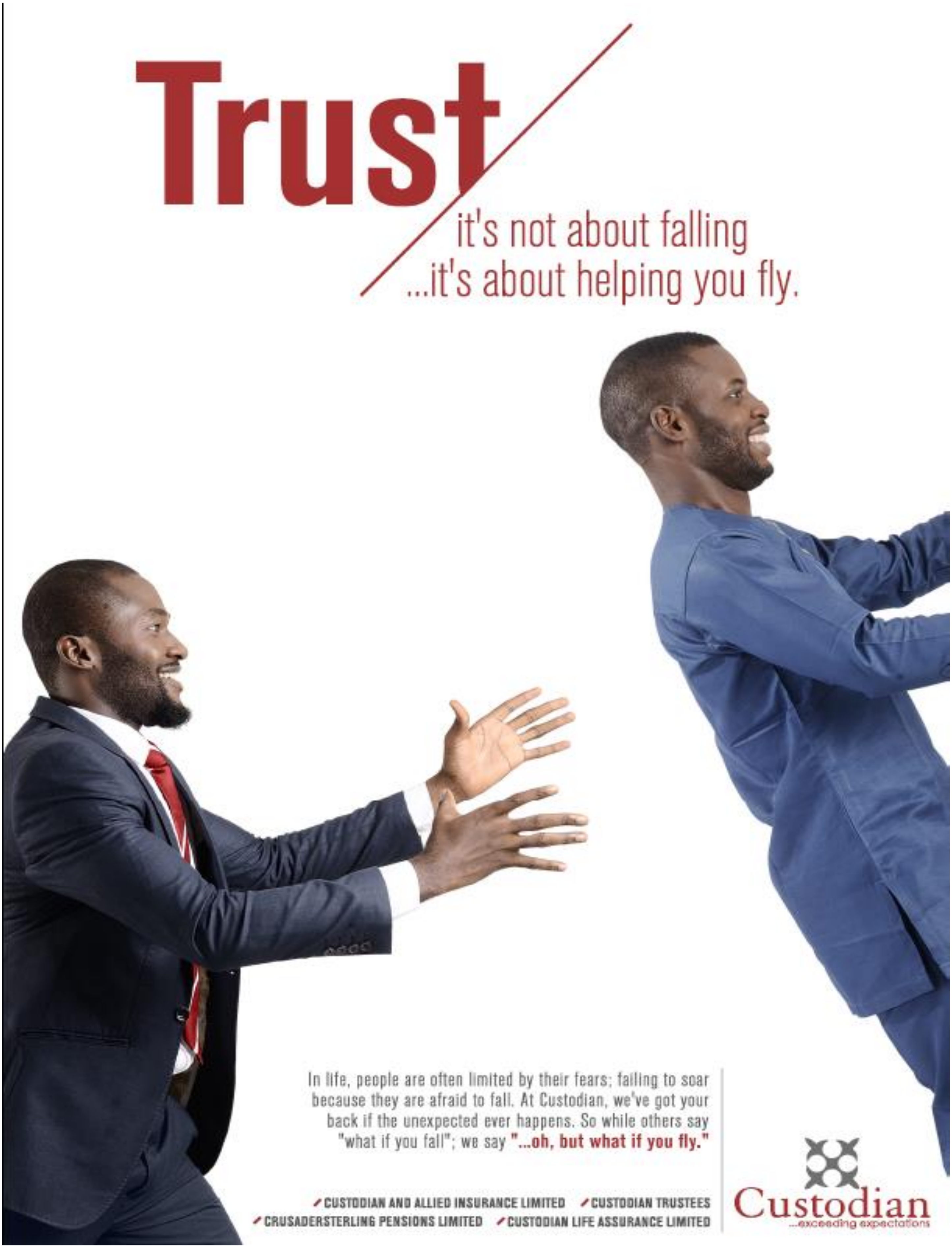
We are forecasting that headline inflation will increase to 11.37% in December from 11.28% in November. If our projections are actualized, it will mean that directionally the change in annual inflation is now becoming a trend. Typically, December is a period in which higher festive related spending pushes up aggregate demand in the economy. Anecdotal and empirical evidence in December 2018 has validated this phenomenon. Compounding the demand pull effect of festive spending was the surge in FAAC by 3.12% to N812.76bn. This means that State Governments and Federal agencies had more liquidity during the period. Also worth mentioning is that the slope of the inflation curve is getting steeper, suggesting that the 2019 budget inflation benchmark of 9.98% may be unattainable. The average inflation rate in 2018 was 12.14% down from16.54%, the 2017 average.



[1]

We anticipate a moderation in monthly inflation (which is more reflective of current prices) to 0.67% (8.36% annualized) from 0.8% (10.02% annualized) in November. This would be driven by higher agricultural output and an increase in manufacturing activities. This rise in manufacturing activity is evidenced by the PMI increase to 60.2 points in December.

[1] NBS, FDC Think Tank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Other inflation moderating factors include: a 1.38% increase in on grid power supply, a 2.23% decline in M2 growth buttressed by a sharp drop of 68.84% in the opening position of banks.

Implications

An uptick in Nigeria's inflation at a time when the US inflation is declining and the US Fed is more committed to interest rate hike tilts the interest rate differential in favor of the US. This increases the probability of naira depreciation. Following the international Fisher effect equation (which states that an exchange rate is expected to change equally in the opposite direction of the interest rate differential) the naira needs to be devalued by at least 10% to keep investors' indifferent. The MPC could also consider a tighter monetary policy stance.

Peer Comparison – 2 greens, 5 reds

Inflation trend was mixed across the sub-Saharan African (SSA) countries under review. Two countries have released their inflation numbers for December - Uganda recorded a decline while Zambia's consumer price index increased. With the exception of South Africa, all the SSA countries under review maintained status quo on monetary parameters at their last monetary policy meetings.

Country	December Inflation (%)		November Policy rate (%)	
Nigeria	11.36**	↑	14	↔
Angola	18.36*	↑	16.5	↔
Kenya	5.58*	↑	9.0	↔
South Africa	5.2*	↑	6.75	↑
Ghana	9.3*	↓	17	↔
Uganda	2.2	↓	10.0 (Dec)	↔
Zambia	7.9	↑	9.75	↔

[2]

[2] FDC Think Tank; *November inflation rate; **December inflation forecast

Outlook

January is usually a slow month and consumer spending typically falls after Christmas. However, the Government has agreed to send the minimum wage bill to the National Assembly on January 23. If the bill is approved, an increase in nominal income and its attendant money illusion effect will boost aggregate demand and prices. This would be one of the major considerations at the next MPC meeting on January 21/22. Being the meeting just before the general elections, we expect the committee members to rely on the slowing monthly inflation rate to justify a dovish approach and thus maintain status quo. Typically, Central Banks usually avoid any changes to monetary policy in the heat of elections.