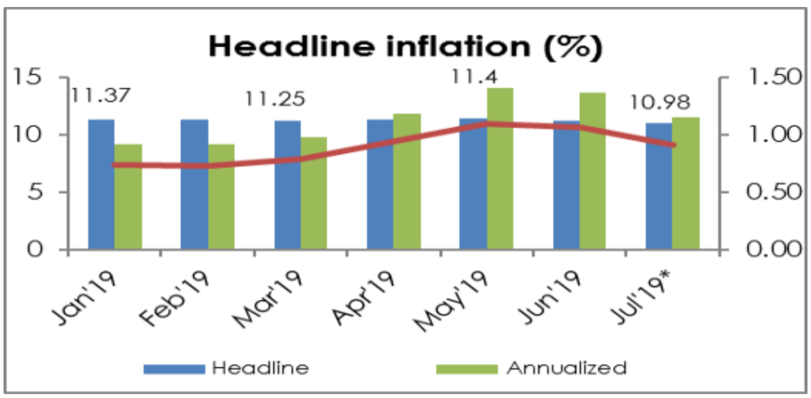
FDC Economic Bulletin

August 09, 2019

Headline inflation to drop to a 42-month low of 10.98%

We are forecasting that the headline inflation in July will slide to 10.98% from 11.22% in June. If accurate, it will be the lowest level since January 2016. The moderation in the general price level would be largely underpinned by lower food inflation due to favourable harvest. Our forecast also points to a 0.16% decline in the month-on-month inflation to 0.91% (11.50% annualized). During our survey in July, we noticed that the prices of most of the commodities in the food basket declined.



[1]

Commodities	Jun'19 (N)	July'19 (N)	% Change
Beans – Oloyin (50kg)	17,000	14,000	17.65
Yam	1,200	1,000	16.67
Tomatoes	20,000	12,000	40.00
Onions	13,000	11,000	15.38
Rice	16,000	16,000	0.00
Garri – Yellow (50kg)	6,250	6,250	0.00

[2]

Even though the projection means the CBN will be closer to achieving its inflation rate of 6-9% target, the probability that headline inflation will fall below 10% and stay there is unlikely at this point in time. This is because the economy will be impacted by the high liquidity resulting from the payment of the new minimum wage to grade 1-4 workers as well as the CBN's effort to boost lending to the private sector.

[1]NBS, FDC Think Tank
[2]FDC Think Tank

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Cost push factors remained subdued in July

In spite of the adjustments in the exchange rate for converting import duty to N326/$, cost push factors were subdued in July, as the prices of white products such as air conditioners, washing machines and dishwashers remained flat. However, the impact of the adjustment could be felt in the coming months.

- The retail price of diesel was down 6% to N222/liter in July. This has reduced logistics and distribution costs by approximately 5%.

- The exchange rate was relatively stable across all market segments in July, supported largely by the CBN's continuous intervention in the forex market ($1.21bn). However, the frequency and amount of intervention in subsequent months could be limited by the steady depletion of the gross external reserves. The gross reserves lost approximately $450mn in the last month, now at $44.69bn.

Minimum wage Impact tapered by a boost in output

The payment of the new minimum wage and arrears for grade 1-4 workers commenced in July. While this is expected to increase purchasing power and boost aggregate demand, its inflationary impact was to a large extent mitigated by the output from the harvests.

Money supply Impact muted

Broad money supply grew by 2.81% to N27.83trn in the month of May. In spite of the CBN's effort to boost liquidity and lending to the private sector, money supply in July was constrained by increased net OMO outflows (N200.10bn). Credit to private sector declined marginally by 0.12% to N24.86trn in May, partly due to high lending rates (21-22% pa).

Outlook

With the commencement of the harvest season, we anticipate a further decline in commodity prices in coming months. This will help taper inflationary pressures from the boost in liquidity due to higher FAAC and minimum wage implementation. The major risk to our projections remains security challenges in the food producing states. The 2-month projections point to a likely inflection as the impact of the arrears on the minimum wage and the implications of the consequential costs on general prices in September.