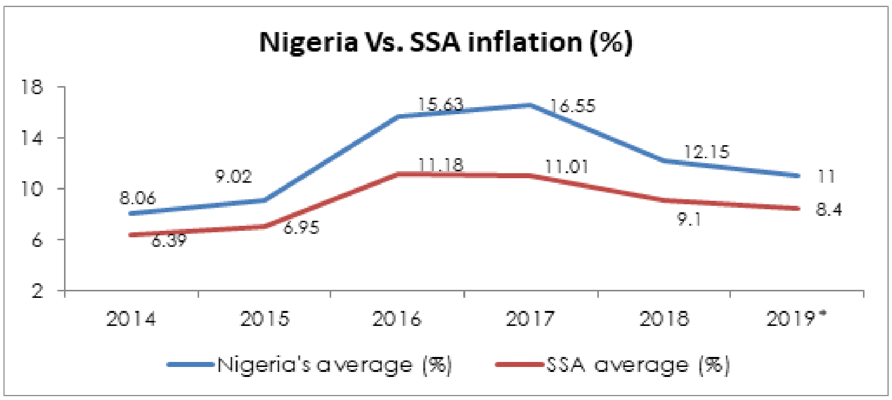
FDC Economic Bulletin

August 19, 2019

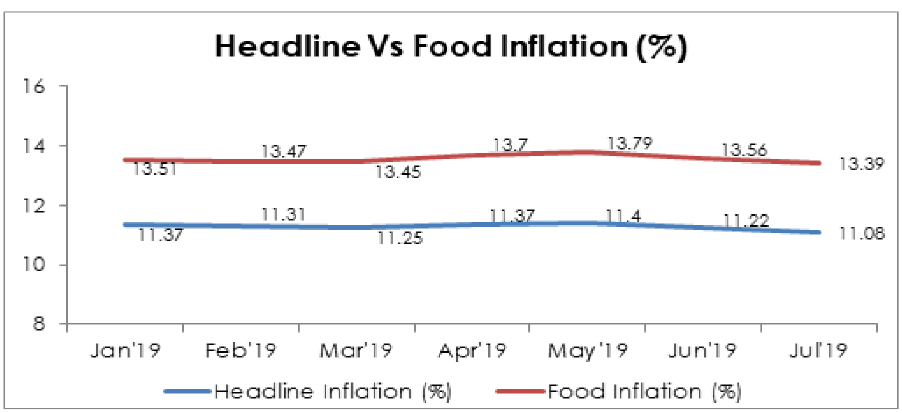
Inflation lower as storm gathers – "Food imports impact not yet in the mix"

The National Bureau of Statistics (NBS) released July inflation numbers on Friday. As was widely anticipated, it declined by 0.14% to 11.08%. Nigeria is now the country with the 8th highest inflation in the African continent. In the region, average inflation in 2019 is projected to be 8.4%. Nigeria's inflation has consistently been above the regional average in the past few years.



[1]

It is worth mentioning that food inflation dropped to 13.39% from 13.56% in June. In the last year, the food basket has been mostly responsible for the direction of inflation. This is because it accounts for more than 50% of the weight in the general basket. The food index declined by approximately 0.60% in the last two months due to a number of factors including a favourable harvest.



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

However, other inflation stoking factors that have been benign are likely to become potent in August and September. These factors include, the minimum wage implementation and the adjustment in the exchange rate for computing custom duty which moved to N326/$ from N305/$. Assuming that 60% of all goods imported attract a duty, the shift from N305/$ to N326/$ will have a pass through effect of approximately N25.7bn.

The apex bank is also contemplating adding dairy products to the list of items restricted from forex. Annual dairy imports is estimated at $1.2bn. In recent times, the President directed the CBN to prohibit forex access for all food imports. This could push up commodity prices and stoke inflation. In Q1'19, food imports was estimated at $1.1bn, 10.7% of total imports. Imported food inflation in Q2 was 15.72%, 2.04% higher than domestic food inflation.

Data Breakdown

Month-on-month inflation slides to 1.01% in July

The month-on-month index, a more accurate measure of price movement slowed to 1.01% (12.77% annualized) in July from 1.07% (13.69% annualized) in June. This was supported by lower food prices as well as a decline in diesel costs. The average price of diesel fell by 6% to N222/ltr in July. This reduced distribution and logistics costs by approximately 5%.

Food inflation dipped by 0.17% to 13.39%

The annual and monthly food indices eased by 0.17% and 0.10%, to 13.39% and 1.26% respectively in July. This was primarily as a result of a favourable harvest. During our survey in July, we noticed that the prices of major food items such as tomatoes, onions and beans declined.

According to the NBS, the price of food items such as bread and cereals increased. However, the global cereal price index declined by 2.7% to 168.6 points in July. These commodities have high import content and are exchange rate sensitive. Thus the adjustment in the exchange rate for computing custom duty to N326/$ from N305/$ most likely pushed up their prices. Imported food inflation rose to 16.39% in July from 15.75% in the preceding month.

The president has directed the CBN to prohibit forex for food imports in order to promote self sufficiency in food production and preserve the forex reserves (which lost $700mn in the last month). Although the move

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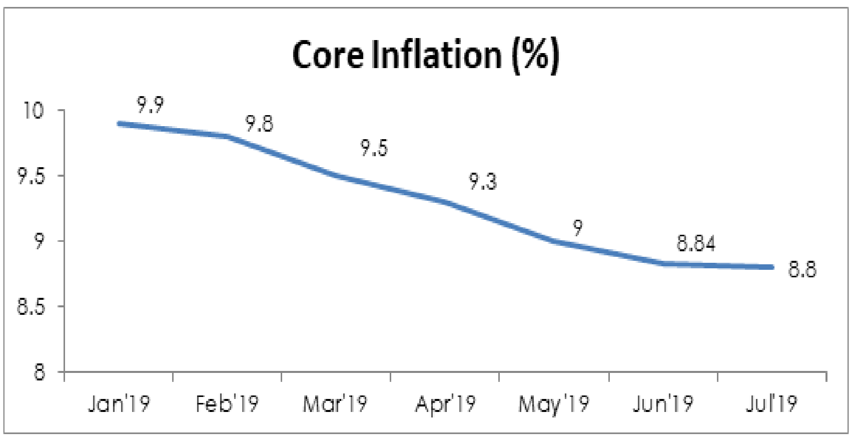
would encourage backward integration and support agric sector growth, it could push up food prices in the coming months as Nigeria is highly food import dependent.

Core inflation down to 8.80%

The year-on-year core index declined to 8.80% in July from 8.84% in June. However, the core inflation curve is flattening out, implying that core inflation is gradually reaching an inflection point. On a monthly basis, it was down 0.08% to 0.77%. This sub-index has benefitted from a relatively stable exchange rate. The naira traded within the tight band of N360-N361/$ at the parallel market. At the IE window, the currency traded within the band of N360-N362/$. The figure shows that the naira is more expensive at the IE window than the parallel window. This has widened the average spread between IE rate and parallel market rate to 0.30% from -0.15% in June. Most transactions are done at the IE window. By implication, we could see a shift to the parallel market, thus, increasing demand pressures. The exchange rate at the parallel market could depreciate to N370/$ in the near term.



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The items that recorded the highest price increases were: medical and hospital services, cleaning, repair and hire of clothing, footwear and household appliances.

Core inflation is 2.34% below the 364-day primary market T/bills rate of 11.14%. This is indicative of a positive rate of return on investment.

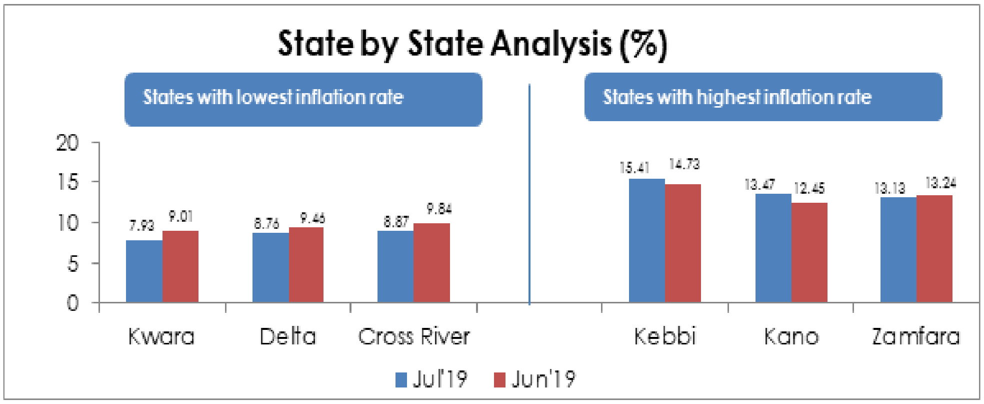
Urban & rural indices sustain downward trajectory

The year-on-year urban and rural inflation rates slowed to 11.43% and 10.64% in July from 11.61% and 10.87% respectively in June. On a monthly basis, both indices dropped by 0.03% and 0.09% to 1.07% and 0.96% respectively.

[3]NBS, FDC Think Tank

State by State Analysis - Kwara, the best performing state

Kwara state had the lowest inflation rate (7.93%), followed by Delta (8.76%) and Cross River (8.87%). Delta state being the only major oil producer in the low inflation category does not confirm any distinct correlation between high oil revenue and low inflation in Nigeria. The states with the highest inflation rates are in the North West – Kebbi (15.41%), kano (13.47%) and Zamfara (13.13%).



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What Next?

Headline inflation in Nigeria has declined in the last two months but is not likely to be sustained as money supply saturation takes it toll and cost push factors add pressure to the price basket. The key issue remains whether the MPC and the CBN are swayed to become more accommodative like most Central banks in the advanced economies.

In contemporary economic thinking which is strongly supported by empirical studies, policy makers are placing greater emphasis on anticipated inflation as against historical data. At Jackson Hole Wyoming this week, Jerome Powell, the Fed Chairman is going to share some of his views and those of big thinkers as to what markets should expect as against what the Twitter in Chief is contemplating.

[4]NBS, FDC Think Tank