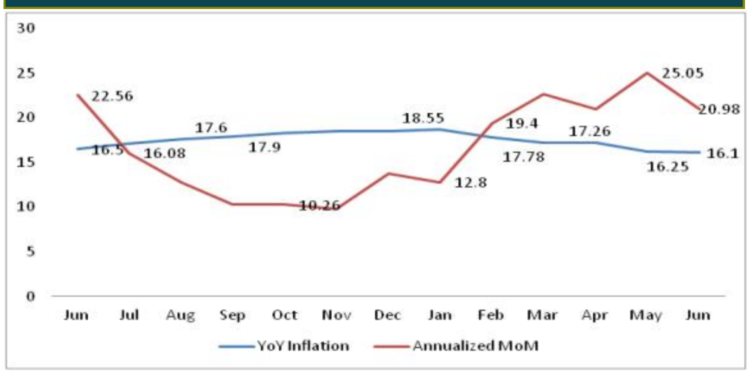
FDC Economic Bulletin

July 11, 2017

Headline Inflation in June to Decline to 16.1%

Year-on-Year headline inflation is expected to decline marginally to 16.1% for the month of June from 16.25% in May, on the backdrop of exchange rate gains and waning base year effects. By this time in 2016, most of the aberrational events had settled, thus making the base year impact minimal. The annualized month-on-month inflation, however, dipped sharply to 20.98% from 25.05% in May. The monthly decline was actually 0.28% to 1.6% in June as against a surge to 1.88% recorded in May.

Chart 1: Headline Inflation vs Month-on-Month Inflation (%)



Source : NBS, FDC Think Tank

Conventional logic suggests that price inflation in Nigeria has been a function of exchange rate volatility. However, in the past few months, the naira has appreciated by 42.08% in the parallel market but manufacturers have failed to pass through the benefits to consumers in the form of lower prices. Therefore we notice a slowdown in price change but no significant decline in the general price level.

The food basket, which is both exchange rate sensitive and seasonal, has remained relatively flat. This is primarily as a result of the planting season, shortages, limited purchasing power and consumer illiquidity. This basket is also responsive to the price of diesel, a major factor in distribution and logistics costs. The price of diesel dropped sharply in June to an average of N160/ltr. Also, storage of perishables is better when temperatures are low, which increases the shelf life of products. The average temperature in Nigeria in June has been 79° Fahrenheit.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Outlook

In general, we see a tapering in the price level due to a combination of factors, notably a stable naira, declining price of diesel, harvest season and switching consumer preferences. We believe that we may be entering into a period of lower consumer prices, as competitive pressures amongst manufacturers and retailers intensify. This trend is reinforced by huge carrying costs due to a high interest rate environment.

A risk that continues to linger is the likely difficulty the CBN may face in supporting interventions in the FX market. Oil prices are expected to sustain a degree of unpredictability, which could mean bad news for Nigeria's FX receipts. In addition, talks about an imposition of a cap on Nigeria's oil production have surfaced. In the event that this manifests, FX receipts and fiscal revenues will decline and will in turn affect the level of FX interventions and budgetary spending.