FDC Economic Bulletin

September 15, 2017

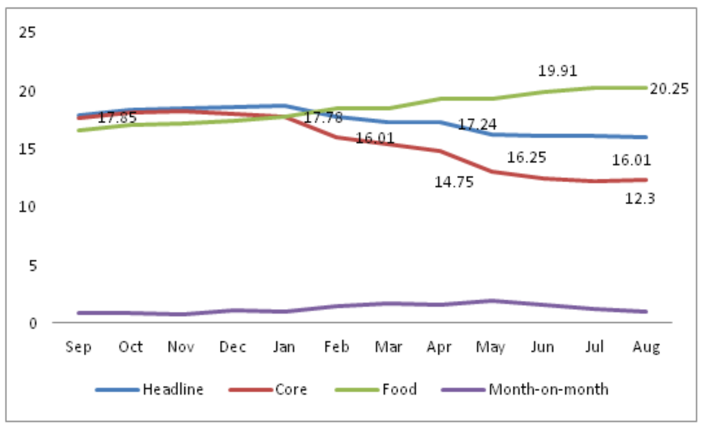
Inflation declines slightly in August to 16.01%

Nigeria's headline inflation numbers were released this morning. As widely expected and consistent with analysts' consensus, the price level slid only marginally from 16.05% to 16.01%. Also noteworthy was the fall in food inflation, which had been the major contributor to the upward swing in the index.

As 2017 progressed, there has been a noticeable reduction in the base year distortions and peculiarities. We have noticed a distinct convergence in the trends of most inflation measures including the food basket, which had been an outlier. Nigeria's food inflation at 20.28% has been at its highest level in recent memory. This was partly as a result of the flash floods in July and the massive disruption to the food supply chain. The economy was quick to recover and food prices have declined to 20.25% in August, as the harvest season kicked in.

GDP growth in tandem

The inflation numbers confirm a trend of declining inflation coinciding with a slow but steady expansion in GDP. Most other proxies and leading economic indicators like the PMI have expanded in July and August. This means aggregate output is increasing at rates higher than money supply growth.



[1]

Core inflation bucks the trend

The data released showed that core inflation, which is price movement after discounting seasonalities, increased to 12.30% in August from 12.20%, its first increase since January. This increase can be attributed to higher domestic and international air fares. In August, IATA rates were reviewed upwards to N325/$ and later to N359/$.

The stunted growth of credit to the private sector at N22.2trn (1.36% YTD) by the increasing risk averse banking community has also constrained output.

[1] NBS, FDC Think Tank

This inflation report offers the last major snapshot of inflation before the MPC meeting coming up on the 25th of September. It will likely influence their decision on whether to move from a tightening cycle towards a more accommodative stance, either symbolically or fundamentally.

The factors that are responsible for the moderation in consumer price inflation include:

- The relatively uninterrupted flow of gas for the powering of on and off grid power. Power supply in August was at an average of 3,350MW and Escravos and Forcados have been without sabotage. This led to the drop in diesel prices to an average of N160/litre.
- Money supply growth has been muted, expanding by 2.43% (month-on-month) to N22.2trn. The slow growth in money supply aggregates, combined with the sterilization of significant portions of money by way of cash reserve ratio deposits, has reduced the velocity of circulation. Therefore the rate of price change has slowed marginally and helped to douse the simmering threat of hyperinflation
- Imported inflation had become a major contributor to the rising price level. For most inelastic products the pass-through rate of the currency devaluation has been higher than 50%. However, for the fast moving consumer goods, the devaluation pass-through is only 30%. Therefore with a stable currency and the naira trading at an average of N367/$ in August, we noticed an indifferent pricing environment with manufacturers not adjusting prices in response to exchange rate movements.

The outlook for inflation in the months ahead is mixed. In September and October, we are expecting a continuation of the slide towards 15.95%. But there is a distinct risk of a reversal of this trend in December as a result of a possible surge in aggregate demand from seasonalities and festivities.