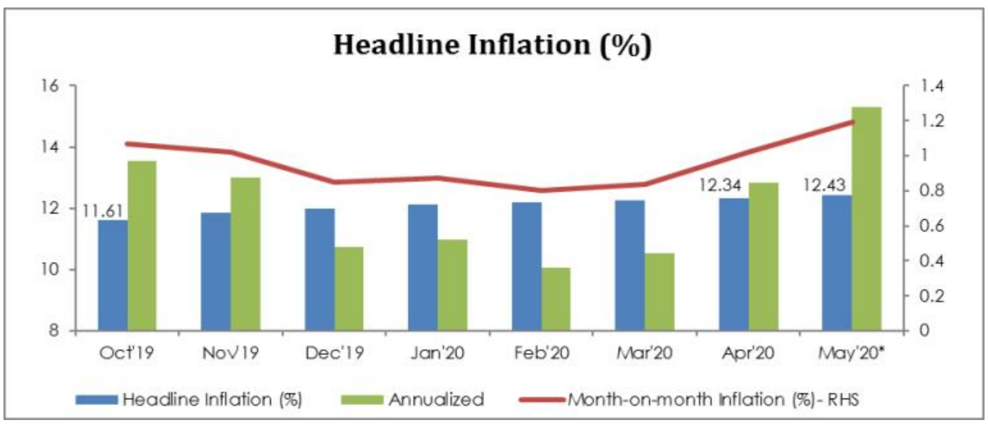
# FDC Economic Bulletin

June 11, 2020

## *Annual inflation to increase again towards 12.50% as monthly inflation jumps to 15.73% (annualized)*

Based on our market survey and regression analysis, headline inflation for the month of May is projected to increase by 0.13% to 12.47%. However, monthly inflation, a more reflective measure of current prices, is likely to spike by 0.21% to 1.22% (annualized at 15.73%). Contrary to consensus expectations that prices will fall as output increases with a partial relaxation of the lockdown, commodity prices surprisingly surged. This was partly due to the combined effects of supply chain disruptions, planting season, higher logistics costs and exchange rate pass through.



[1]

### Noticeable Trends

- **Surge in the retail price of commodities that are price inelastic**

  We noticed a surge in the retail prices of commodities such as tomatoes, pepper and onions, that are relatively price inelastic. The price surge was primarily due to the planting season effect and higher logistics costs.

| | Apr'20 | May'20 | % Change |
|---|---|---|---|
| **Tomatoes** | 8,000 | 12,000 | 50 |
| **Pepper** | 7,500 | 13,000 | 73.33 |
| **Onions** | 13,000 | 20,000 | 53.85 |

[1]NBS, FDC Think Tank

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- **Higher logistics costs: A major recipe for price differential**

In recent times, the reduction in the number of passengers that buses can carry has forced an abnormal spike in transportation fares. This has resulted in price differential between the markets. The farther the markets are from the production points, the higher the chances of been impacted by rising logistics costs. On the average, commodity prices are approximately 15% higher in Sura market than Oyingbo.

| | Sura | Oyingbo | % Difference |
|---|---|---|---|
| **Rice (50kg)** | 28,000 | 28,000 | - |
| **Beans (oloyin)** | 17,500 | 17,000 | 2.94 |
| **Yellow garri (50 kg)** | 15,000 | 13,600 | 10.29 |
| **Semovita (10kg)** | 3,800 | 3,400 | 11.76 |
| **Margarine** | 900 | 900 | - |
| **Cornflakes** | 700 | 600 | 16.67 |
| **Bornvita** | 1200 | 1200 | - |
| **Lipton** | 300 | 300 | - |
| **St Louis Sugar** | 700 | 600 | 16.67 |
| **Melon seeds** | 800 | 400 | 100 |

- **Lower petrol price failed to translate to higher aggregate demand**

Many analysts had anticipated an increase in aggregate demand due to the 14.83% reduction in the pump price of PMS. The impact of this was however muted by the sharp fall in consumers' disposable income due to the covid-induced economic paralysis.

- **Commodity prices remained high in spite of a fall in disposable income**

A fallout of the Covid-19 pandemic and the lockdown measures was a significant loss in jobs and a drop in aggregate disposable income. According to the NBS, the Covid impact monitoring report, 42% of the respondents have lost their jobs due to the Covid-induced economic crisis while 79% confirmed that their disposable income has fallen. In reality, this is expected to translate to lower aggregate demand as well as a shift in the consumption pattern. Although, it is believed that lower aggregate demand will lead to a fall in commodity prices, the supply-side shocks triggered an increase.

## Impact on consumers

- **Lower purchasing power and living standards:** As inflation rises, the cost of living increases. This, at a time when aggregate disposable income is falling, implies that consumers' purchasing power as well as standard of living will reduce, especially for low-income earners.

[2] NBS, FDC Think Tank

- **Reduction in private savings:** Higher inflation points to a possible reduction in private savings. This is because a larger proportion of consumers' income will be spent on necessities such as food. Also, rising inflation discourages savings as the real value of money saved declines.

## Impact on policy makers and businesses

At the last MPC meeting, the monetary policy rate was reduced by 100bps to 12.5%p.a, citing the need to strike a balance between price stability and output recovery. The continued rise in inflationary pressures increases the chances of a rate hike at the next meeting. Higher interest rates will increase borrowing costs and slow down the rate of domestic investment. However, foreign portfolio investments are likely to rise as interest rates increases. This will provide some support for the country's external reserves as well as the exchange rate.

## Peer Comparison – Mixed movement in Inflation – 4 Reds, 3 Greens

Three of the Sub-Saharan Africa (SSA) countries under our review have released their inflation numbers for the month of May. While Kenya and Uganda recorded a decline, Zambia posted an increase. The primary driver of the inflationary trend across the SSA countries has been the food price movement alongside currency adjustments.

Nigeria, like most other SSA countries reduced its benchmark interest rates by 100bps to 12.5%p.a. at its last meeting. This however is just a signaling move as the last rate cut in March had a muted impact on the market.

| Country | May Inflation (%) | May Policy rate (%) |
|---|---|---|
| Nigeria | 12.6 (April forecast) | 12.50 |
| Angola | 20.81 (Apr) | 15.50 |
| Kenya | 5.47 | 7.00 |
| South Africa | 4.1 (Mar) | 3.50 |
| Ghana | 10.6 (Apr) | 14.50 |
| Uganda | 2.8 | 7.00 (Jun) |
| Zambia | 16.6 | 9.25 |

## Concluding Thoughts

Headline inflation will most likely continue its upward trajectory in the coming months mainly due to supply constraints. This will be compounded by the new electricity tariffs, which is expected to kick-in on July 1. The fall in aggregate demand could however slowdown the rate of increase.