FDC Economic Bulletin

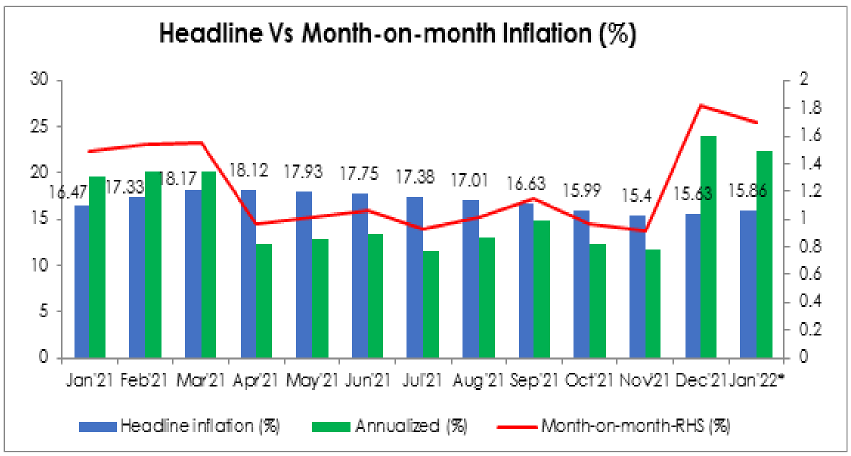
February 10, 2022

Inflation—Negative surprise as valentine's day draws close

The NBS will release its inflation report on February 15. After seven consecutive months of decline and one increase last month, official headline inflation is projected to rise again by 0.23% to 15.86%. If this projection is correct, it means Nigerian inflation will be moving in tandem with global trend. For instance, US inflation spiked again to 7.5% (highest inflation rate in 41 years). It is now almost imminent that the US Fed will hike interest rates by 50 basis points next month.

In Nigeria, one of the causative factors of inflation in this period is the depreciated naira pass-through into domestic prices. This is having a cross elasticity effect on local substitutes. Typically, commodity prices decline at the beginning of the year due to the harvest and the post-Christmas blues. This time around, the fall in prices is not as much as in the previous years. The blended rate for foreign exchange purchased is effectively N560/$ and even the supposed boost in locally produced commodities have import contents.

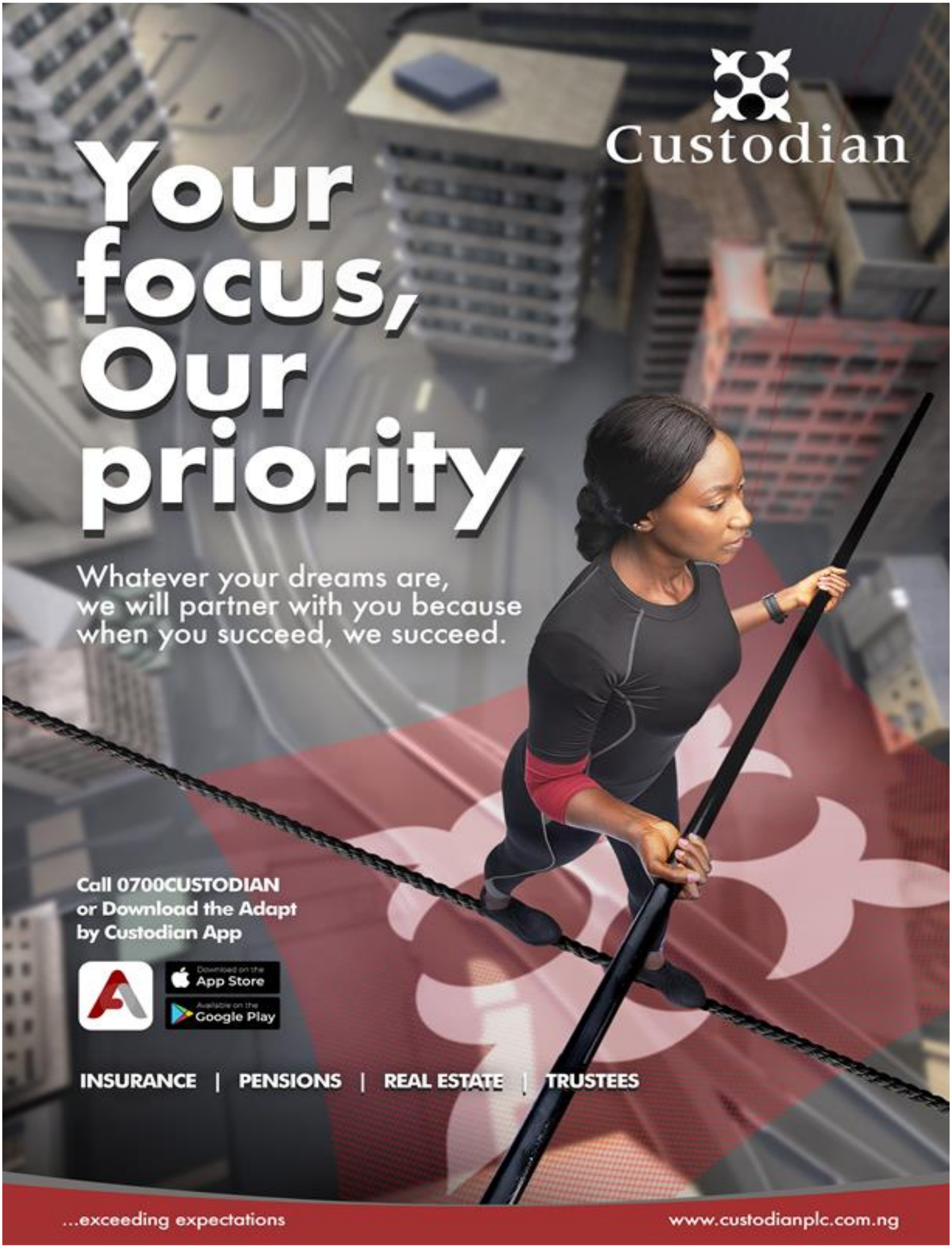
Another important factor is the effect of excess naira liquidity (ways and means advances) and low interest rates on the general price level. This could further mount pressure on the currency.



[1]

We allude to the fact that inflation expectations are tilted in favour of an unexpected increase in price inflation. The markets had already come to accept the fact that petrol price was bound to increase in February. The delay in the implementation of this policy only led to confusion in the mind of analysts and market operators. The price of diesel spiked by 20% to N410-420/litre from N350/litre a week ago. This will drive up food transportation costs in the short-term and further threaten price stability.

[1] NBS, FDC Think Tank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Data Breakdown

Monthly inflation to fall by 0.12% to 1.70% (22.43% annualized)

Month-on-month inflation is expected to decline to 1.70% (22.43% annualized) from 1.82% (24.07% annualized) in December 2021. This is partly because of lower aggregate demand due to post-Christmas blues.

Food and core inflation to remain elevated

Based on our model, the annual food and core inflation (inflation less seasonalities) sub-indices are expected to increase in January 2022. Food inflation is projected to rise by 0.64% to 18.01% while core is estimated to increase by 0.33% to 14.2%. This will be largely driven by cost pressures (exchange rate pass through, higher energy and logistics costs), supply chain disruptions and output shortages.

Other policy considerations

IMF urges Nigerian government to implement major reforms

While economic reforms/polices are intended at driving market efficiencies and eliminating distortions, the timing of such reforms/policies has a significant impact on its success or failure. The IMF, in its Article IV review re-iterated the need for major reforms in the fiscal space, exchange rate, trade, and governance to boost long-term, inclusive growth. The government could be put under pressure to implement these reforms especially in a pre-election year.

Boosting government revenue through taxes – impact on aggregate demand

The Federal Inland Revenue Service (FIRS) has announced the resumption of tax payment on income derived from bonds and short-term securities. This is coming barely one month after the introduction of a 6% digital tax on foreign e-commerce businesses and a N10/liter excise duty on all carbonated, non-alcoholic and sweetened beverages. It therefore highlights the government's quest to boost its domestic revenue generation. However, it will have a negative impact on the attractiveness of short-term government securities and reduce aggregate demand.

Sub-Saharan African – Inflation falling amid higher energy prices

It appears that inflation in the African continent is beginning to defy global trends. Of the 10 African countries that have released their inflation report for January 2022, 7 recorded declines while 3 posted increases. This is despite the uptick in global oil prices (currently at a record high of above $90pb). Inflation tapering factors in these countries defer. In Kenya, lower price inflation was largely as a result of government interventions in the power and petroleum sectors, which helped to keep energy prices stable. Despite the removal of fuel subsidy by the Zambian government in Dec'21, inflation continued its trend downwards. This suggests that the interest rate hike in the preceding month helped to taper cost pressures.

Country	January Inflation (%)		Most Recent Policy rate (%)	
Nigeria	15.86*	↑	11.50	↔
Angola	27.03 (Dec)	↑	20.00	↔
Kenya	5.4	↓	7.00	↔
South Africa	5.9 (Dec)	↑	4.00	↑
Ghana	13.9	↑	14.50	↔
Uganda	2.7	↓	6.50	↔
Zambia	15.1	↓	9.00	↑

Inflation outlook – impact on policy decisions

The MPC will be meeting again next month to decide on the monetary policy direction. If the upward inflation trajectory is sustained (January/February), the MPC could be forced to bite the bullet and increase the MPR by at least 50bps. However, the Q4'21 GDP data will be released before the meeting (Feb 22). If the numbers come in lower than expected, the committee will be stuck between a rock and a hard place.