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CONTENT

TINUBU

TINUBU 1.0: REFORM GRENADES AND THE MARKET FORCES

On taking the oath of office on May 29, 2023, Mr. Bola A. Tinubu, Nigeria's 16th president, said, inter alia, "the question we now ask ourselves is whether to remain faithful to the work inherent in building a better society or retreat into the shadows of our unmet potential. For me, there is but one answer. We are too great a nation and too grounded as a people to rob ourselves of our finest destiny". There is no doubt that Mr. Tinubu's speech will stand in history as one of the most patriotic inaugural speeches since the commencement of the fourth republic. Such a great speech could come from long-nurtured dreams or visions, which could translate to great goals and incredible outcomes. However, talk is cheap, they say. It can either be a dream come true or a dream marred by pushbacks. Nonetheless, it's during wars that generals are made!

From subsidy removal to the promise of housecleaning at the CBN and exchange rate unification, the market has responded with a good nod. The market is a good rewarder of those that diligently do its bidding, but it could be vicious in punishing those that go against its dictates. It is a ruthless king. In the words of Ludwig von Mises, "*the market economy ... does not respect political frontiers. Its field is the world*". The market expectation is that the subsidy removal will be sustained, multiple currency practices will be scrapped, fiscal consolidation will be prioritized, pro-investment reforms will be emphasized, and sustainable and balanced growth will be given preeminence. Indeed, Mr. President seems to have sacrificed his presidential honeymoon for reform grenades.

However, there could be pushback. Nigeria is known for political clientelism and entrenched vested interests.

1 The Economic Times (August 10, 2016). Monetary policy is like juggling balls; have said no to many powerful people: Raghuram Rajan. https://m.economictimes.com/news/economy/policy/monetary-policy-is-like-juggling-balls-have-said-no-to-many-powerful-people-raghuram-rajan/articleshow/53632915.cms

now elected, it is expected that President Tinubu will submit the list of nominated cabinet members for legislative screening. It is believed that the choice of cabinet members will determine whether the reform momentum will be sustained or not.

PETROL SUBSIDY REMOVAL

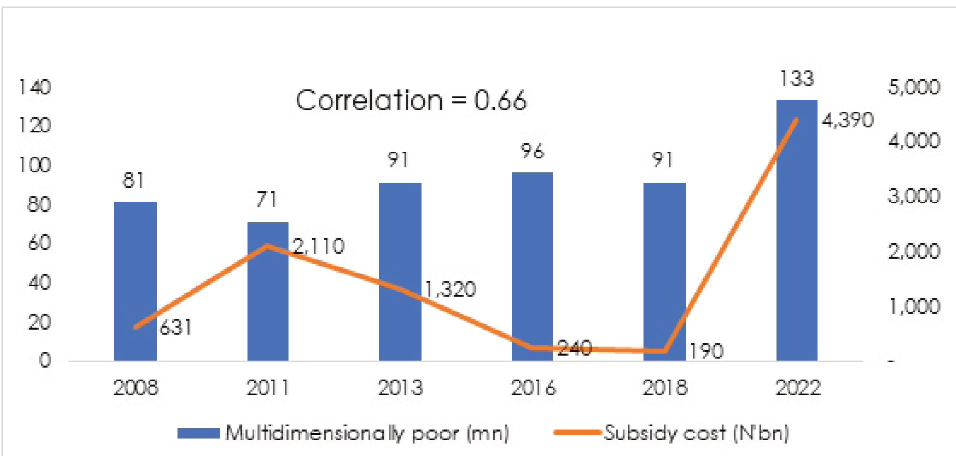
The President announced that "fuel subsidy is gone" during his inaugural speech. He explained that fuel subsidies are no longer sustainable and that there is a need to re-channel the wasteful spending into productive expenditures such as public infrastructure, education, and health care. Although many analysts considered this bold and decisive, the immediate market reaction was mixed. Nigeria's equities market gained N1.51 trillion after the announcement of the removal of petrol subsidy, with the all-share index rising by 5.2% to 55,738.35 and market capitalization spiking to N30.3 trillion from N28.8 trillion. Also, Nigeria's dollar bond market rallied, with the longer-term bonds increasing by about 2%, its highest gain in one month.

Nigeria's subsidy regime epitomizes monumental waste and inefficiency, with available evidence showing that the total subsidy bill in 2022 (N4.39 trillion) exceeded the budgets of about 21 states put together. It also exceeded FGN 2022 capital expenditure (N1.893 trillion) by about 132%. There is no doubt that subsidizing 66 million liters of petrol per day, out of which 44 million liters were smuggled, is a deadweight loss.

However, a nation with 133 million (63%) multidimensionally poor citizens and only about 45% of its citizens connected to the national grid will, no doubt, face a pushback to subsidy removal. However, as Figure A.1 clearly shows, subsidy spending seems to worsen rather than ameliorate the poverty incidence in Nigeria.

Tinubu had barely finished the announcement when the dealers began hoarding petroleum products, resulting in long queues at petrol stations. The NNPC then rolled out a new list of petrol price, with differentiated pricing across states. Currently, petrol sells for between N488 and N550 per liter, representing more than 150% price hike.

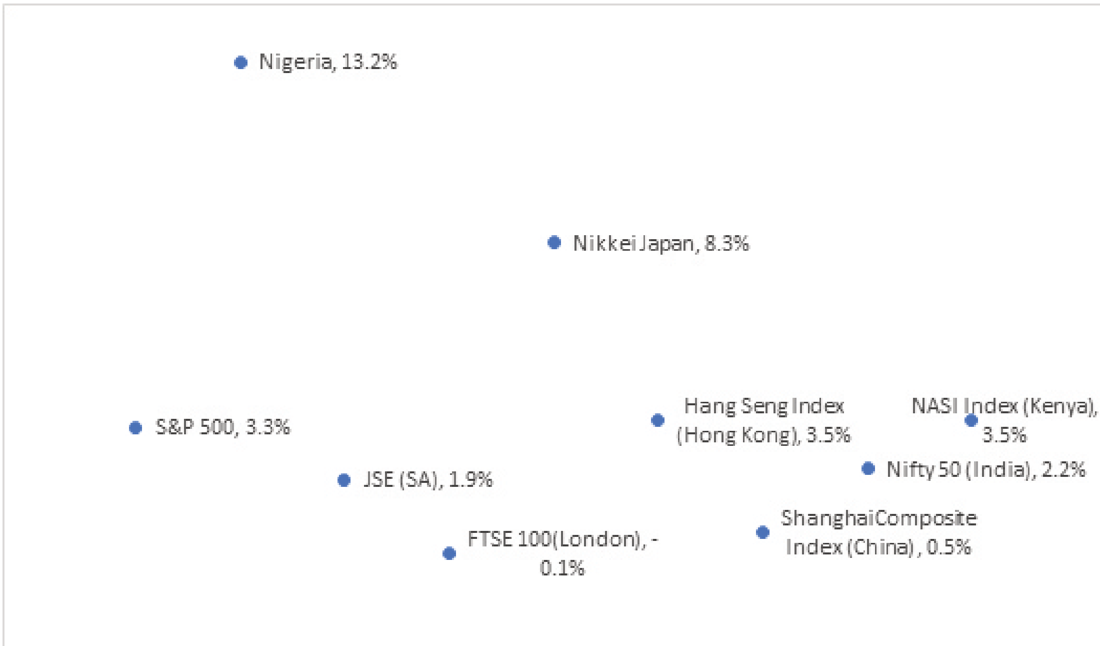
FIGURE A.1: POVERTY INCIDENCE VS SUBSIDY SPENDING



Source: FDC

2 Mann, C.L. (February, 2023). Expectations, lags, and the transmission of monetary policy. https://www.bankofengland.co.uk/-/media/boe/files/speech/2023/february/expectations-lags-and-the-transmission-of-monetary-policy-speech-by-catherine-l-mann.pdf

STOCK MARKET PERFORMANCE ACROSS THE GLOBE (MAY 26-JUN 14)



Source: Mann (2023)

TThe government will also need to demonstratively prove to the citizens that the savings from subsidy removal will be invested in productive infrastructure that will have a direct positive impact on households in the long run. This notwithstanding, the government must immediately communicate its palliative plans to cushion the effect of subsidy removal on the populace.

MONETARY POLICY HOUSECLEANING

The President promised to initiate housecleaning exercise of the monetary authorities. The implementation of monetary policy in the past decade has been anything but stellar. Many analysts argue that the central bank is not independent and politically detached. The monetary policy framework of the central bank (in practice, not in principle) can best be described as unclear. The goal of monetary policy is generally to achieve price stability while also promoting sustainable economic growth and full employment. Price stability is the primary goal, while full employment and sustainable growth goals are secondary.

In what seems to be the beginning of the housecleaning exercise as promised, the CBN governor, Mr. Emefiele, was suspended and subsequently arrested for questioning by the security operatives. Following the suspension of the apex bank chief, the bond and equities markets rallied on Monday and Tuesday this week, respectively. On Monday (June 12), the Nigerian dollar bond outperformed other emerging market bonds. Bloomberg reported that the dollar bonds maturing in 2051 rose more than 3% to as high as 73.74, the biggest gain this year. According to the JPMorgan index, the premium investors demand to hold Nigerian debt over US Treasuries fell by 46 basis points to 710, the biggest drop year-to-date. Similarly, the Nigerian stock market jumped by 4% on Tuesday (June 13), the first trading day after the suspension of the CBN governor. Since the inauguration of President Tinubu, the Nigerian equities market has outperformed its peers, gaining 13.2% in the past two weeks.

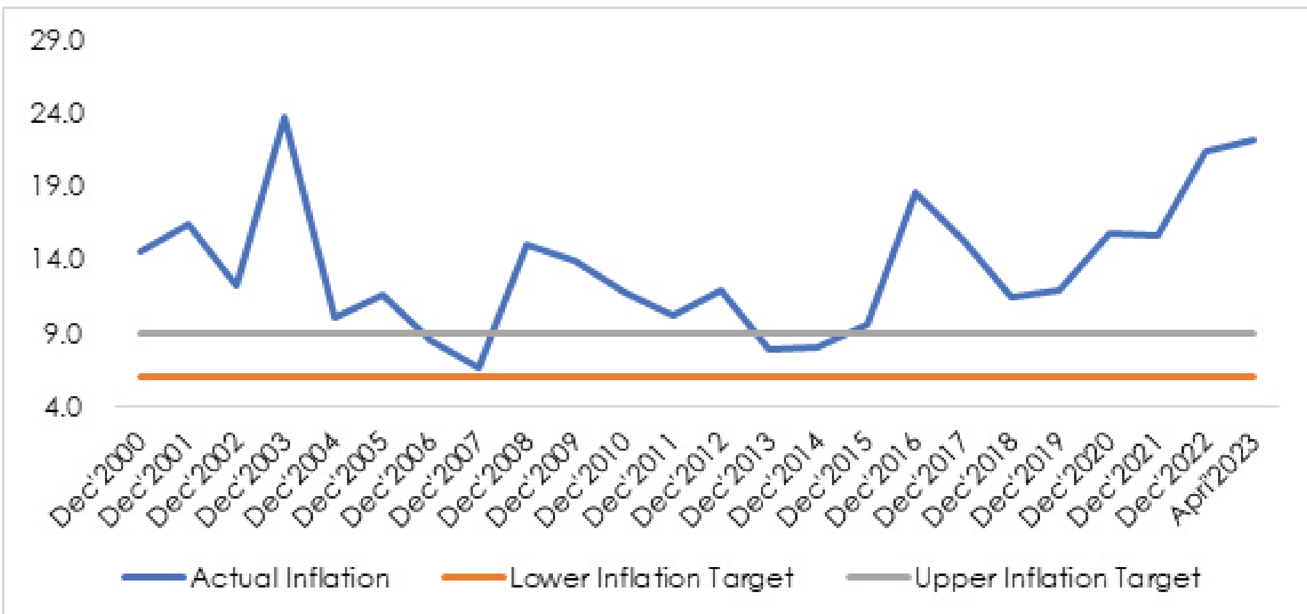
Redefining the monetary policy framework

One of the areas the housecleaning exercise should focus on is redefining the monetary policy framework. A monetary policy framework, which is a set of principles and strategies that guide a central bank in conducting monetary policy, plays a crucial role in the effectiveness of monetary policy. These frameworks include inflation targeting, exchange rate targeting, money supply targeting, and interest rate targeting. First, the CBN needs to be clear on what its primary mandate is: price stability, low unemployment, or economic growth. The CBN cannot be a jack of all trades! A clear and well-defined mandate can help guide the central bank's decisions and communicate its policy objectives to the public, which can increase the credibility of its actions and help anchor inflation expectations.

The CBN also needs to be clear on its monetary policy framework: explicit inflation targeting, implicit inflation targeting, exchange rate targeting, or money supply targeting. A well-designed framework can help ensure that the central bank's monetary policy decisions are transparent, credible, and consistent over time, which can enhance the effectiveness of its actions in achieving its policy objectives. Currently, the CBN has a flexible inflation rate of 6–9%. Since 2000, Nigeria has never met the lower band of the target (6%). The upper band of the target (9%) was also exceeded, except in 2006, 2007, 2013, and 2014.

The effectiveness of monetary policy also depends on a number of factors, including the structure of the financial system and the transmission mechanism of monetary policy. Operating a tight monetary policy and, in the same breath, monetizing government debts and "sharing intervention funds" is, no doubt, a recipe for disaster.

FIGURE A.2: ACTUAL VS TARGETED INFLATION



Source: FDC

UNIFIED EXCHANGE RATE AND LOW INTEREST RATE

Tinubu had said he would ensure low interest rates and unified exchange rates. First, the interest rate is a number; it is determined by economic fundamentals such as demand for money, supply of money, and inflationary pressure. To achieve low interest rates without the Turkish experience will require achieving low inflation first. Nigeria's inflationary pressure is driven by exchange rate passthrough, energy prices, money supply saturation, fiscal deficit monetization, and supply shocks.

Recently, the CBN announced the adoption of the "willing-buyer-willing-seller model" as well as a single exchange rate window. This new exchange rate framework is expected to increase transparency in the forex market, reduce exchange rate risks and transaction costs, and buoy investor confidence. However, exchange rate unification cannot be achieved by announcing an exchange rate as the unified rate. No! There must be a systematic and coordinated program for achieving unification through convergence. If the exchange rates are unified at the parallel market rate of N750/$ or the purchasing power parity rate of N685/$ and the restrictions are removed, there could be increased forex inflow through the official channel. The ease in forex demand pressure at the parallel market could strengthen the naira.

However, beyond announcing a unified rate, exchange rate management must prioritize forex demand and supply fundamentals over administrative control. It must be noted that the autonomous market is a "black market". It is not a creation of the law but of a market supply-demand gap. If the exchange rate arbitration cabals are not dismantled, devaluing the exchange rate may not be a silver bullet.

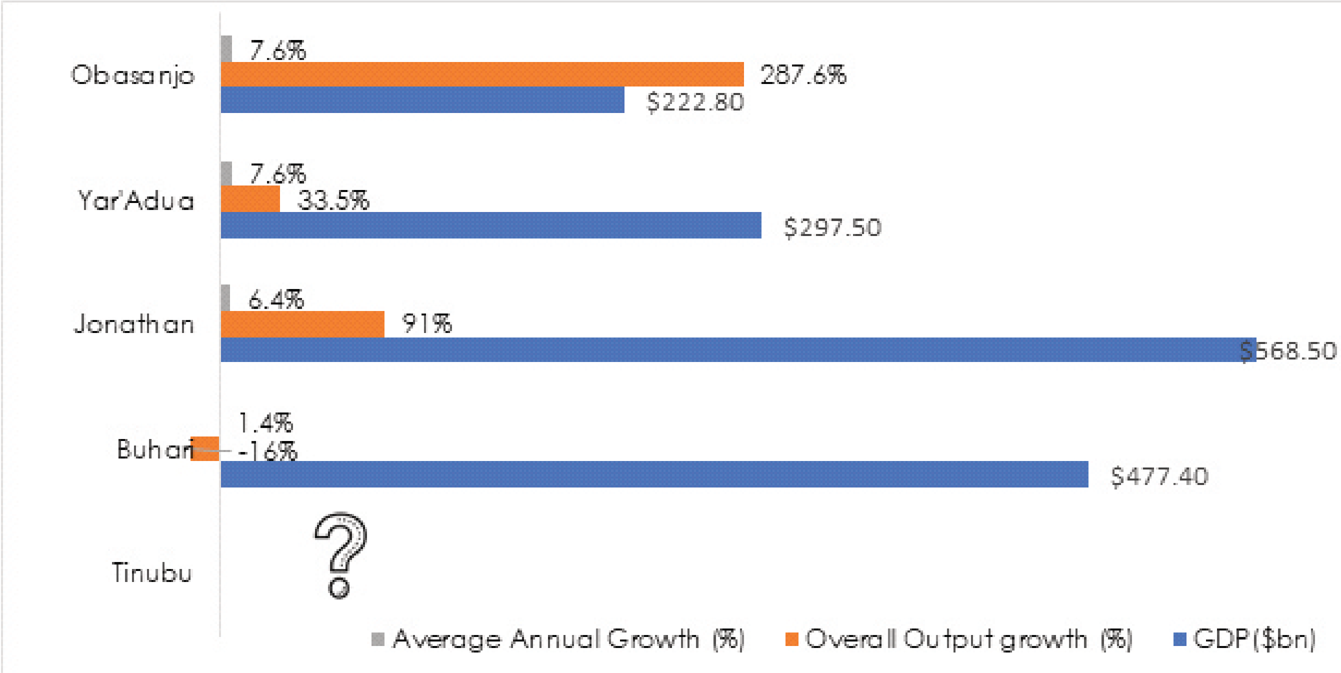
ECONOMY

On the economy, the president promised to "target higher GDP growth and to significantly reduce unemployment". It's no brainer to know that Nigeria needs output growth as much as one needs air. After growing the economy at an annual rate of 7.6%, 7.6%, and 6.4% under Obasanjo, Yar'Adua, and Jonathan, respectively, the economy stagnated at an average annual growth rate of 1.4% under Buhari's administration. In fact, in dollar terms, the output level fell to $477.4 billion under Buhari's administration from $568.5 billion under Jonathan's administration in 2014. In the eight years of Obasanjo's administration, the national output rose by 287.6% to $222.6 billion from $57.5 billion in 1999.

Although Buhari's administration was confronted with several headwinds, including dwindling oil prices (2014–2017), the COVID-19 lockdown (2020), and the Russia–Ukraine war (2022), there is no doubt that the economic management under his watch was poor and disoriented. Economic growth was partly dwarfed by heightened macroeconomic instability, including a currency crisis, spiraling inflation, stagnating total factor productivity, a forex market crisis, dwindling revenue, and a ballooning debt profile.

Some of the structural constraints that have undermined economic activity in the past eight years include worsening insecurity, a dearth of requisite infrastructure (e.g., electricity, roads, etc.), an obstructive labour market, and endemic corruption. The president had identified some of the priority constraints to deal with, viz., electricity, industrial, and budgetary reforms.

FIGURE A.3: OUTPUT LEVEL AND ECONOMIC GROWTH ACROSS DIFFERENT ADMINISTRATON

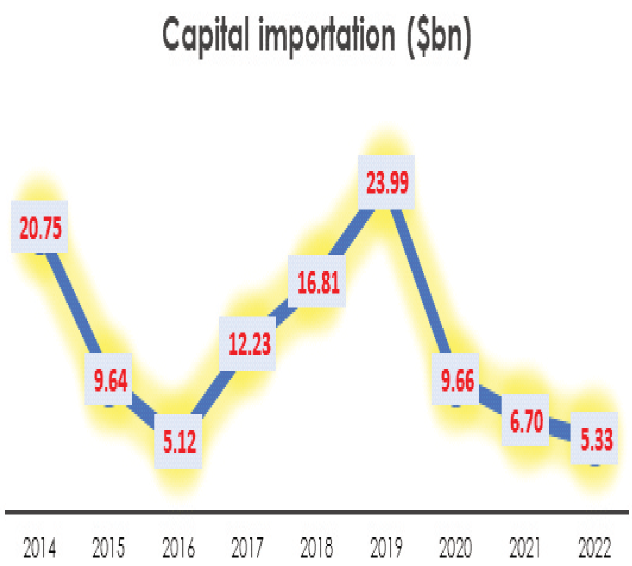


Source; FDC

Note: to avoid overlapping, we used the GDP in the penultimate year to the end of the administration to represented the output level left behind by a president. The overall output is obtained by comparing the GDP in the first year and the GDP in the penultimate to the last year. The value of the GDP in dollar is used to make for meaningful comparison by adjusting for exchange rate effect.

.In recent times, the industry has faltered, contracting by 0.5% and 4.7% in 2021 and 2022, respectively. To spur growth, Nigeria must focus on export-led, investment-led, and balanced growth. The government must be ready to deal with economic and regulatory terrorists who are committed to frustrating the government's reform agenda for personal aggrandizement.

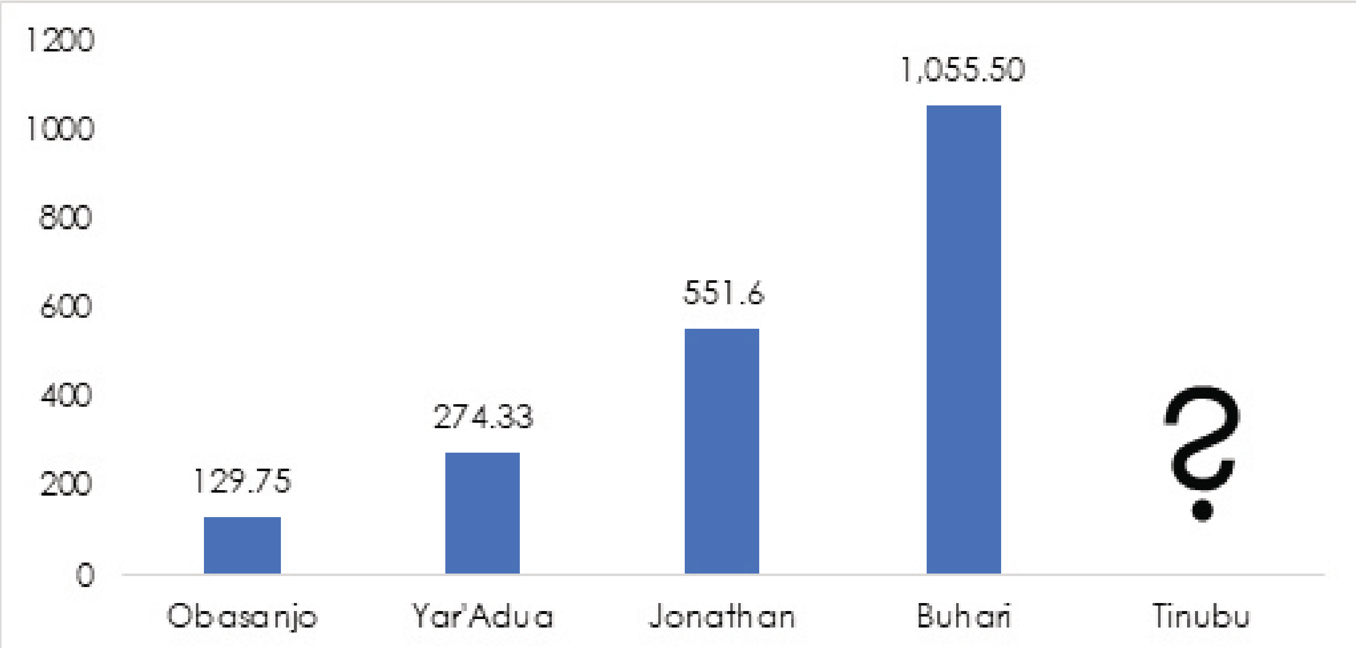
The ugly trend of dwindling foreign investment must be reversed, not just by taking advantage of capital flow push factors but by focusing on the pull factors.



1 Push factors refer to economic or financial conditions in the country of origin of the capital that make it less attractive or desirable to hold capital there. These factors may include political instability, economic recession, high inflation, currency devaluation, or poor investment opportunities. When these conditions worsen, investors may seek to move their capital out of the country, which can lead to capital inflows into the recipient economy. This is susceptible to capital flow reversals. On the other hand, pull factors refer to economic or financial conditions in the country of destination of the capital that make it more attractive or desirable to invest there. These factors may include political stability, strong economic growth, low inflation, a stable currency, or attractive investment opportunities. When these conditions improve, investors may be attracted to invest in the country, leading to capital inflows.

3 Danish Refugee Council (March, 2023). Global Displacement Forecast 2023. https://pro.drc.ngo/media/4c5hxa5c/230310_global_displacement_forecast_report_2023.pdf

FIGURE A.4: AVERAGE SECURITY SPENDING (DEFENSE + INTERNAL SECURITY) PER ANNUM (N'BN)

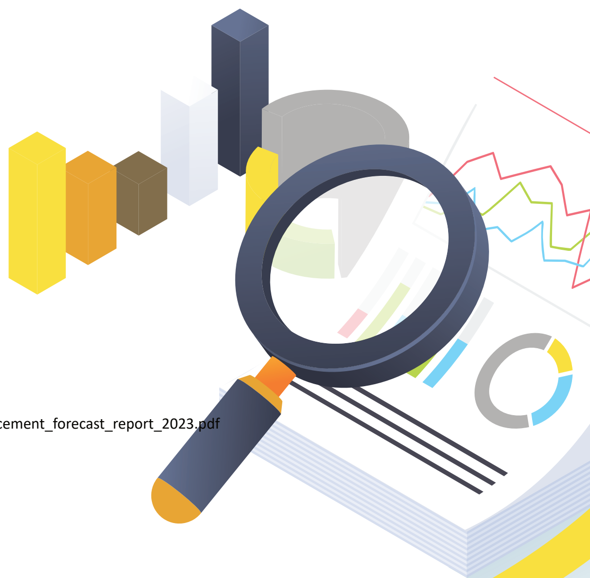


Source; CBN, FDC

SECURITY

On security, Mr. Tinubu said, "*security shall be the top priority of our administration... We shall invest more in our security personnel, and this means more than an increase in number. We shall provide, better training, equipment, pay, and firepower*". In the past 13 years, Nigeria has been battling worsening insecurity. In 2022, it was ranked the 6th most terrorized country in the world. According to the Nigeria Security Tracker, a total of 63,111 non-natural deaths were reported in the past eight years as a result of banditry, Boko Haram, and other outlawed non-state actors.

Nonetheless, government security spending has increased geometrically in the past decade. With about 370,000 police officers (or a police-to-citizen ratio of 1:580) and nearly 230,000 military officers (or a military-to-citizen ratio of 1:930), there is no doubt that Nigeria is relatively under policed. Investment in military armament is imperative. However, the government must go far beyond the business-as-usual practice of spending money without getting value for such expenditure. Beyond equipment and recruitment, the security architecture must be overhauled. The 3.6 million farmers who are currently displaced in Nigeria need to return to their farms. The security KPI must move from expenditure to incidence of insecurity.



Global Terrorism Index (2022). https://www.visionofhumanity.org/wp-content/uploads/2022/03GTI-2022web.pdf

Nigeria Security Tracker (2023). https://www.cfr.org/nigeria/nigeria-security-tracker/p29483

Danish Refugee Council (March, 2023). Global Displacement Forecast 2023. https://pro.drc.ngo/media/4c5hxa5c/230310_global_displacement_forecast_report_2023.pdf

LAGOS

ECONOMIC IMPLICATIONS OF LAGOS TRAFFIC CONGESTION – THE NEED TO CREATE ALTERNATIVES

Around the world, traffic congestion foretells challenges for the efficient flow of people and products. On the aggregate, the global economy is losing around 10% of its output due to traffic congestion every year.[4] Lagos, the largest commercial hub in Nigeria, is regarded as the city with the highest traffic congestion in the world when it comes to getting delayed in traffic on the way to and from work. Lagos state reported a traffic index of 348.69, greater than the 344.06 for Los Angeles (2nd), and 331.12 for San Jose (3rd). This is according to the most recent statistics made public in June 2022 by Numbeo, the largest cost-of-living database in the world.[5,6]

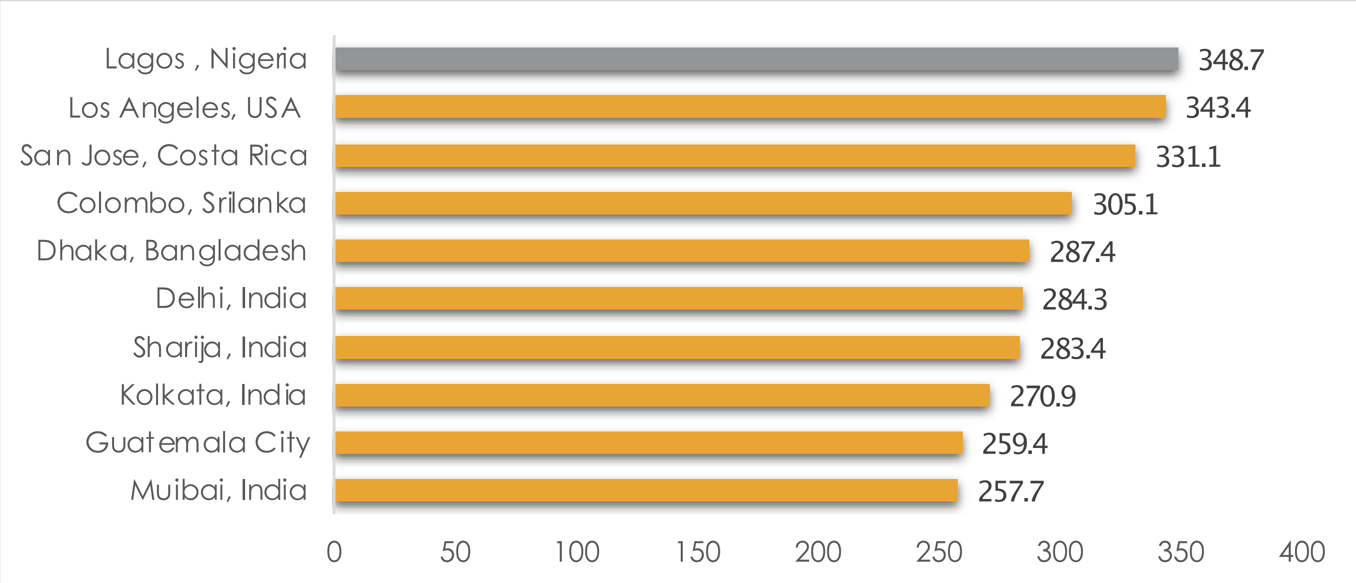
Some of the main causes of the state's heavy traffic congestion include its large population density, inadequate road infrastructure, and an over-dependence on road transportation and personal vehicles. Approximately 1.8 million vehicles use Lagos roads annually as of 2022 and Lagos has 226 automobiles per km, which is more than the global average of 11 cars per km and the national average of 16 cars per km.[7]

THE COST IMPLICATIONS OF LAGOS TRAFFIC

In 2019, the Danne Institute for Research, in partnership with the Financial Derivatives Company, estimated the financial and economic costs of Lagos traffic congestion for individuals and businesses. The research concluded that on average, Lagosians lose three productive hours commuting to work daily.[8] Assuming that these lost hours remain constant, Africa's fourth-largest economy loses N10.39 trillion ($22.48 billion) in GDP every year due to traffic congestion. Consequently, the Lagos state government is losing N520.34 billion of internally generated revenue. [9]

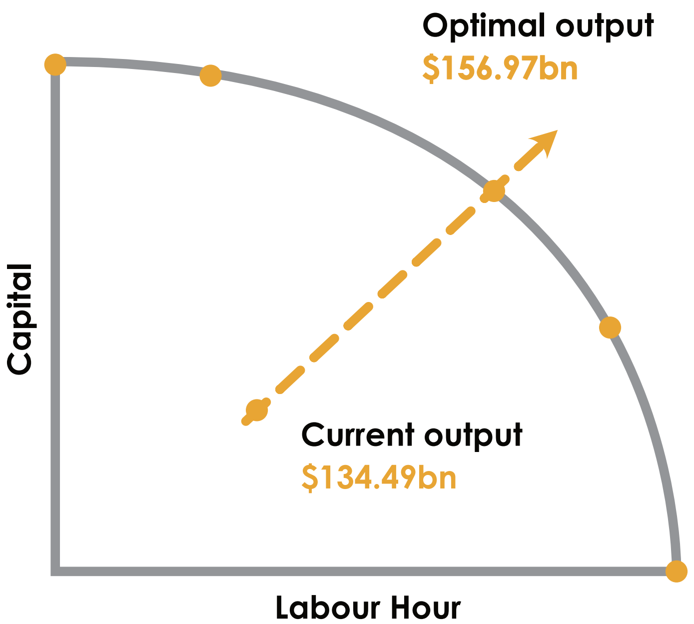
4 INRIX Global Traffic Report, 2022. https://inrix.com/scorecard/
5 The Traffic Index is, by definition, a composite index of the amount of time spent in traffic owing to commutes to work, the estimation of time consumption displeasure, the estimation of the amount of CO_2 that is used in traffic, and the overall inefficiencies in the traffic system.
6NUMBEO. 2022. "Traffic Global Traffic Indices". https://www.numbeo.com/traffic/rankings.jsp?title=2023&displayColumn=0
7 Thisdaylive.com/index.php/2022/05/17/transportation-sector-largest-emitter-of-greenhouse-gases-lagos-govt-laments/
8 https://arbiterz.com/lagos-loses-n4-trillion-to-traffic-congestion-annually
9 In 2022, the Lagos State government generated 5% of the state GDP in internally generated revenue, hence 5% of lost output (5%*$22.49 bn) is $1.13 billion. With the exchange rate of N463/$, the state economy is losing N520.34 billion in revenue.

FIGURE B.1: TRAFFIC INDEX



Source: Numbeo and FDC Think Tank

FIGURE B.2: LAGOS STATE POTENTIAL OUTPUT VERSUS ACTUAL OUTPUT[10,11]



Beyond time lost, the average Lagosian spends more than 45% of their annual income on transportation.[12] In addition to this sizable economic loss, there are also numerous externalities associated with congestion that have not yet been identified, such as the effects on public health due to excessive air pollution during times of congestion. According to the Lagos state government, the transportation sector accounts for more than 60% of the greenhouse gas emissions in the state.

10 Labour hour is ineffective as a result of productive hours lost in traffic, weakness, and health challenges from CO2 emission in traffic
11 Capital is less productive due to wastage especially fuel burn in traffic
12 Lagos State Government. Household Survey Report (2020). https://lagosstate.gov.ng/wp-content/uploads/2022/02/Y2020-Household-Survey-Report.pdf

THE WATER TRANSPORTATION SYSTEM – AN ALTERNATIVE AND COMPLEMENTARY OPTION

Water transportation is appealing for Lagos. Around 40% of the state is made up of water bodies. Lagos has approximately 8 lagoons that extend for 210km along the coast and exist alongside tidal wetlands and swamps. Lagos and Lekki lagoons are the largest. Others include Yewa, Badagry, Ologe, Iyagbe, Kuramo, Apese, Epe, and Mahin lagoons.[13] The Lagos Lagoon alone is between three and 13 km broad; it is more than 50 km long; and for the most part, hosts smaller barges and boats, with the exception of the Commodore Channel which can hold ocean-going ships.[14]

The importance of water transportation in Lagos state traffic congestion management cannot be overstated. In addition to alleviating traffic congestion when used as a supplement to roads, water transportation is also more sustainable in terms of energy use, noise, and gas emissions.[16]

Inadequate infrastructure is one of the key barriers to water transportation in Lagos. With over 21 million inhabitants, Lagos is a densely populated city, yet its water transportation system is still underdeveloped, with insufficient jetties, terminals, and navigational aids. Another issue is the underfunding of water transport infrastructure, which has caused both the absence of new facilities and the deterioration of already existing ones. Water hyacinth, a plant that grows quickly in water, is also a significant hindrance to water transportation in Lagos as it clogs up rivers and slows down boat traffic. Finally, the low level of awareness among the populace about the potential benefits of water transportation has also contributed to its underdevelopment.

Lagos State Wetlands Map: MDPI 15

13 Badejo O.T & Alademomi A. 2014. "Tidal Characteristics and Sounding Datum Variation in Lagos State". International Journal of Innovative Research Studies. https://docplayer.net/195054469-Tidal-characteristics-and-sounding-datum-variation-in-lagos-state.html
14 https://www.researchgate.net/figure/Lagoons-and-Water-Bodies-in-Lagos-State_fig1_273699298
15 https://www.mdpi.com/2304-8158/11/24/3987

16 researchgate.net/publication/306344802_Analysis_of_Intra-City_Water_Transportation_in_Lagos_State/link/57b8a53b08ae14f440bb4d62/download

LESSONS FROM ISTANBUL'S WATER TRANSPORTATION SYSTEM

Instanbul Water Bus

Turkey's capital, Istanbul, is encircled by sea on all sides. With more than 50% of Istanbul covered by water bodies, it has become known for its public water transportation system. In the early centuries of Istanbul (formerly Constantinople), the city was known for its well-developed road network and horse-drawn carriages. In the late 19th and early 20th centuries, the introduction of horse-drawn trams, followed by electric trams and buses, helped alleviate some of the congestion on Istanbul's streets. However, by the mid-20th century, Istanbul's rapidly growing population and an increasing number of vehicles led to serious traffic problems in the city centre.

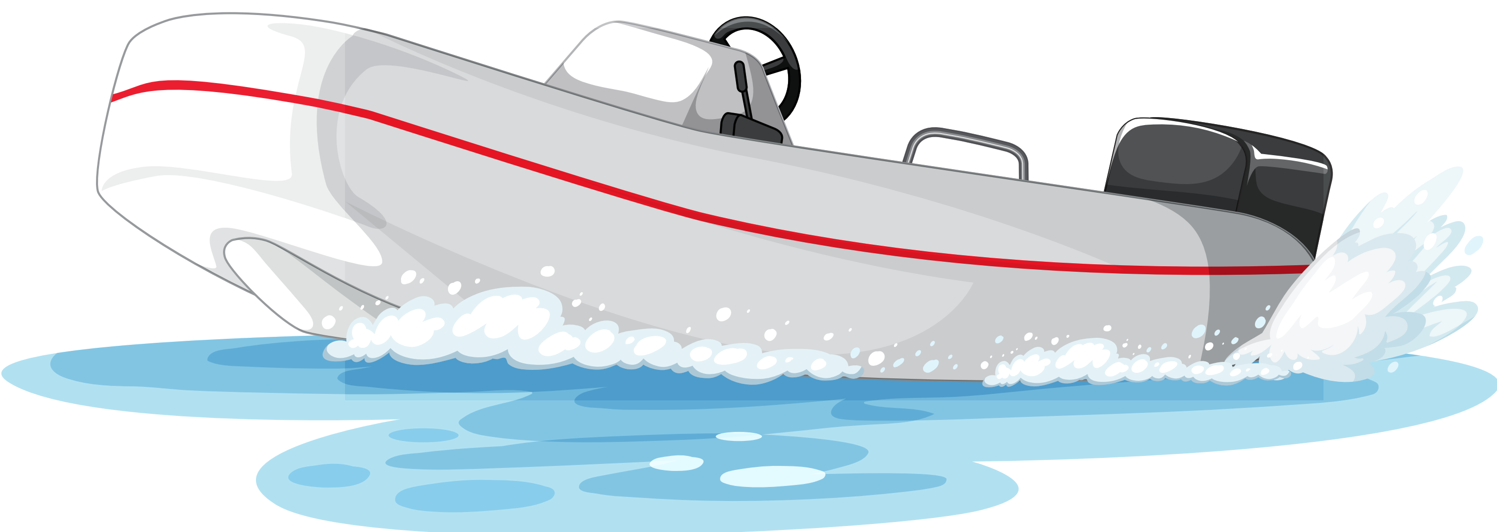
The development of public water transportation, particularly the ferry system, played a significant role in improving transportation options and reducing traffic congestion in Istanbul. One of the key initiatives taken by the Istanbul Metropolitan Municipality (IMM) was the development of a public ferry network in 1958. The ferry network operates on the Bosphorus, the Golden Horn, and the Marmara Sea, and connects various neighbourhoods and districts across the city. The ferry network is affordable, and efficient, and provides a comfortable and scenic ride for commuters. Today, the ferry system remains a vital component of Istanbul's transportation infrastructure, with millions of passengers using the ferries each year to travel between the European and Asian sides of the city, as well as to the city's many islands and coastal districts.

Another initiative taken by IMM is the promotion of private water transport. The city has made it easier for private boat owners to obtain permits to operate water taxis and water buses and has also developed new marinas and docking facilities to support private water transport.

INVESTING IN LAGOS WATER TRANSPORTATION SYSTEM

The Lagos state government needs to do everything it can to encourage investment in water transport. For example, the N1.8 trillion budgeted for the construction of the fourth mainland bridge could instead be used to upgrade the waterway, which would be a more effective method of reducing traffic. Another option could be dredging the wetlands that surround the state to allow the use of ferries and sea buses. This could serve as a better alternative to the already overstressed road transportation system.

The economic implication of creating alternative or complementary options to the road transportation system in Lagos state is profound. In addition to having the capacity to add an estimated N6.93 trillion to Lagos' economy, water transportation as an alternative would reduce the commuting hours of Lagosians, mitigate the health implications of traffic on the people, increase productivity, improve the standard of living, and reduce unemployment. If Lagos could successfully implement a water transportation system it may even have a shot at improving tourism revenue. In all, water transportation presents better alternatives to the already traffic-congested road transportation system in Lagos state.



GLOBAL

GLOBAL PERSPECTIVE

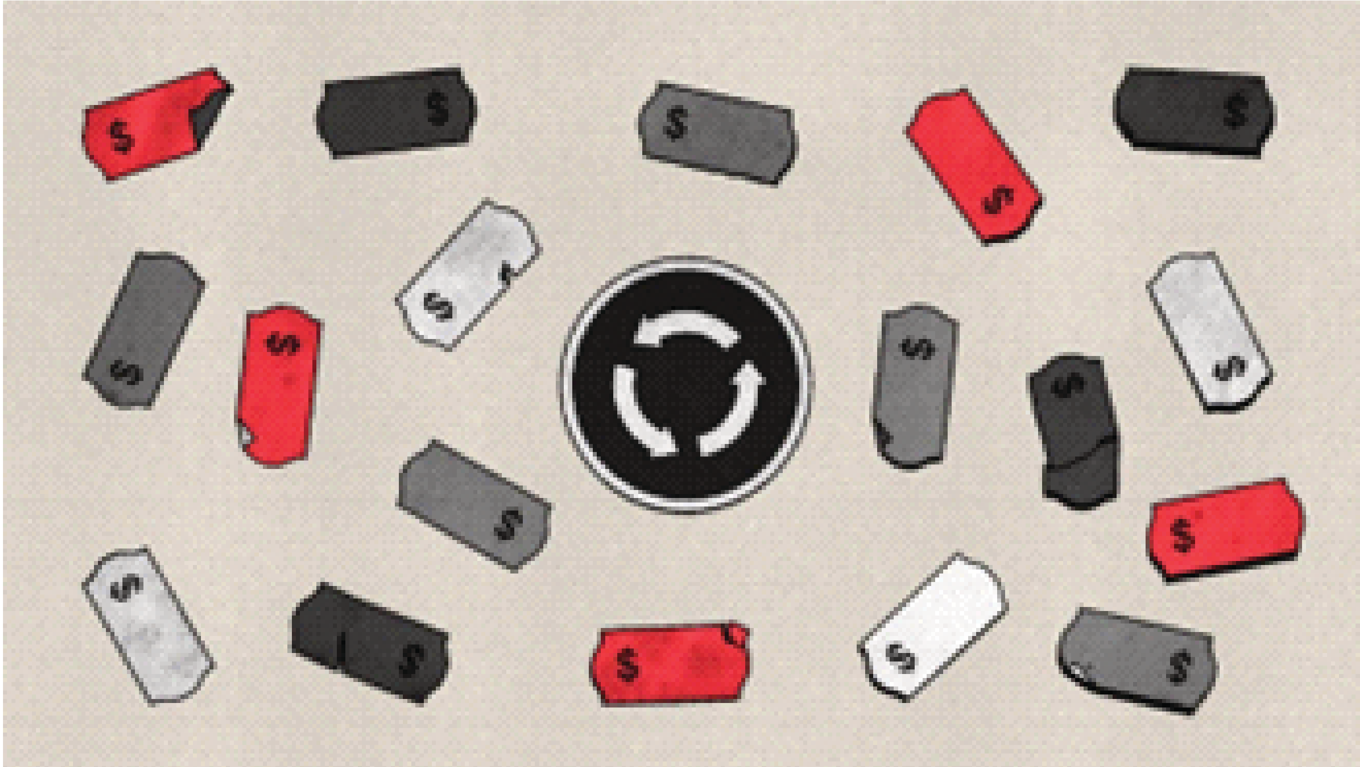
WAGE- PRICE SPIRALS ARE FAR SCARIER IN THEORY THAN IN PRACTICE –

CULLED FROM THE ECONOMIST

A wage-price spiral is the stuff of inflationary nightmares. It refers to a situation when prices gallop higher—perhaps because of a sudden shock or policy missteps, or both—and wages race upward to keep pace with them, in turn feeding through to yet more price rises and yet more wage increases, and so on in a vicious circle. It can seem as if the world's economies have been living this horror: in America hourly earnings rose by about 6% last year, the biggest annual increase in four decades. In Britain wages excluding bonuses are rising at an annual clip of about 7%. On June 14th, when the Federal Reserve elected to leave interest rates unchanged after ten consecutive increases, Jerome Powell, its chairman, warned that he was watching wage trends as one test of whether the central bank might resume raising rates in July.

But the dangers that appear in nightmares usually bear little resemblance to the threats worth worrying about in reality. The world's uncomfortable ride with inflation over the past two years seems to point to a similar conclusion about wage-price spirals: they are a caricature of what happens to an economy with an inflation problem.

The historical parallel often trotted out in discussing wage-price spirals is the 1970s. Price and wage inflation seemed to interact throughout that decade, much as the spiral framework suggests. Each surge in general price inflation was followed by a surge in wage inflation, which was followed by more price inflation—and on it went. But the 1970s are flawed as evidence for the existence of spirals. The repeated waves of inflation stemmed more from successive oil-price shocks (in 1973 and 1978) than from prior wage gains. To the extent that wages and prices moved in lockstep, this reflected trade unions' practice back then of pegging salaries to the cost of



Rising salaries are a poor predictor of future inflation

living, guaranteeing a ratchet effect. Spirals were a feature of contracts rather than proof of an economic concept.

Late last year a group of economists at the IMF interrogated the historical record, creating a database of wage-price spirals in advanced economies dating back to the 1960s. Applying a fairly low bar—they looked for accelerating consumer prices and rising nominal wages in at least three out of four consecutive quarters—they identified 79 such episodes. But a few quarters of high inflation is not all that scary. A few years is far more frightening. Judged by this longer standard, the IMF economists offered a more upbeat conclusion: the "great majority" (they omitted the exact percentage) of short-term spirals were not followed by a sustained acceleration in wages and prices.

In a note in March, Gadi Barlevy and Luojia Hu, economists with the Fed's Chicago branch, took a closer look at the role of wages in the current episode of inflation. They focused on "non-housing services", a category that covers everything from car washes to medical check-ups and which Mr. Powell regularly cites as a useful indicator because of its tight association with wages. Mr. Barlevy and Ms. Hu concluded that wages do help to explain this segment of inflation: nominal wage gains have outstripped productivity growth by a sizeable margin over the past year. Facing that cost squeeze, service providers would naturally want to raise prices.

For years such projects were regarded as technically plausible, perhaps, but uneconomical. An influential estimate by the American Physical Society in 2011 put the cost of dac at $600 per tonne of CO_2 captured. By comparison, permits to emit one tonne currently trade at around $100 in the eu's emissions-trading system. ccs has been a perennial However, the spiral thesis claims not merely that wages matter, but that they predict future inflationary trends. On this count, the Chicago Fed economists found the relationship unidirectional: inflation helps to forecast changes in labour costs, but changes in labour costs fail to predict inflation. Service providers, in other words, raised prices before rising wage costs hit their bottom line. Mr. Barlevy and Ms. Hu posit that employers may have been ahead of the curve in anticipating predict future inflationary trends. On this count, the Chicago Fed economists found the relationship unidirectional: inflation helps to forecast changes in labour costs, but changes in labour costs fail to predict inflation. Service providers, in other words, raised prices before rising wage costs hit their bottom line. Mr. Barlevy and Ms. Hu posit that employers may have been ahead of the curve in anticipating the effects of a tight labour market. That makes wages a lagging, not a leading, indicator for inflation.

Adam Shapiro, an economist with the San Francisco Fed, has been even more critical of the wage worries. In a note in May, he isolated unexpected changes in wages to argue that rising labour costs were only a small driver of non-housing service inflation and a negligible one in broader inflation. Like his Chicago colleagues, he concluded that wage growth was following inflation.

None of this means that wage-price spirals are a total myth, which some overeager commentators have written. As the IMF's study noted, serious spirals can occur; it is just that they are extremely unusual. Were inflation to stay very high for a long time, people might start to view fast-rising prices as a basic fact of life and incorporate that assumption into their wage demands. It is possible that this process has begun in Britain.

But in America what is striking about the past two years is how relatively moderate inflation expectations have remained, despite price pressures. In a paper last month for the Brookings Institution, a think-tank, Ben Bernanke, a former chairman of the Fed, and Olivier Blanchard, a former chief economist of the IMF, decomposed the drivers of pandemic-era inflation. They concluded that a triumvirate of shocks (commodity-price spikes, strong demand for goods and supply shortages) accounted for most of the inflation overshoot since 2020. There was scant evidence that inflation itself had triggered higher wage demands. Wages shot up simply because demand for workers outstripped supply.

Dreaming spirals

Wages and prices can be driven up by the same force: excessive spending in the economy compounded by shortages of both products and the workers to produce them. Overheated economies are worth worrying about regardless of whether prices and wages are feeding on each other.

For their part, Messrs Bernanke and Blanchard argue that as pandemic shocks fade away, overheated labour markets are likely to contribute more to inflation. To stop that, central bankers need to make sure that the demand for workers cools off. Only if inflation persists once the labour market is back in balance will fear of a self-sustaining spiral be worth losing sleep over.

GLOBAL

GLOBAL PERSPECTIVE

LOOKING FOR THE AFRICAN MIDDLE CLASS? HEAD TO THE BUS PARK—

CULLED FROM THE ECONOMIST

The Ugandan traffic officer slid back the door of the 14-seater taxi to find 20 adults, four children, and a squashed *Economist* correspondent. "Why are none of you complaining?" she asked, peering into the tangle of limbs. Indeed, nobody had said anything as the conductor had delayed departure to stuff his minibus beyond legal limits. And now they kept quiet as the policewoman ordered the excess passengers to disembark. A mile down the road, with the cops out of sight, the evictees squeezed back in again, having hitched a ride on tactically positioned motorbikes.

The policewoman's question is pertinent. Why should African travellers put up with discomfort and delay? Shared taxis and intercity buses routinely leave hours late. Most passengers tolerate bad service with surprising equanimity. But some of them are starting to demand a better one—a sign of rising incomes and the changing economic value of time.

Public transport in Uganda often tests patience. Your correspondent once sought a ride from a taxi park in Lira, a northern town. "Hurry, hurry," urged a tout, steering him towards a packed vehicle with a revving engine. Ten minutes later, with the taxi still motionless, a passenger stepped out to "buy a soda" and never returned. A quarter of an hour passed, and another did the same, then another. It eventually became clear that almost all the "passengers" were paid stooges, enticing customers with the illusion that the taxi was full and ready to leave.

The answer to the policewoman's question is given by Huzairu Lubega, who manages a bus company.

New "executive" services promise comfort and punctuality

Buses with fewer than 45 passengers cannot cover the costs of fuel and maintenance, he says, so they wait for hours for extra travellers. The only way to leave on time would be to raise the price of tickets. Passengers accept delays because they understand this trade-off, and are too pinched to pay for a faster service. When most people are hard up, late departures are the market equilibrium.

But as incomes rise, so does the opportunity cost of waiting around. In January Global Coaches, which runs to the prosperous city of Mbarara, launched an "executive" bus service in response to customer demand. Travellers pay a third more than the usual fare in return for air conditioning, larger seats, folding tables and complimentary water. Even better, the bus leaves on time. "You know the schedule so you can plan your day properly," says Pius Mugabe, an engineer with a window seat. Without wishing to sound "fancy", "you are seated with people you can relate to".

This kind of premium service is already well established in wealthier African countries. Some Kenyan bus companies offer an earthbound version of the airline experience, replete with on-board Wi-Fi, refreshments, a "business-class" section and cavernous VIP seats. Their customers are not the moneyed elite, who are chauffeured about in oversized Toyota Prados. Instead, they are an emerging class of salaried workers and small-businesspeople who cannot afford to drive but still have meetings to attend on time.

Scholars have spilled much ink debating the size of the African middle class. Some definitions are so broad as to encompass almost anyone who is not living in poverty. Others count only the affluent minority who live a Western lifestyle. But another way to understand class is through the subtle markers of social distinction. Just look for a punctual departure and a bit of leg room.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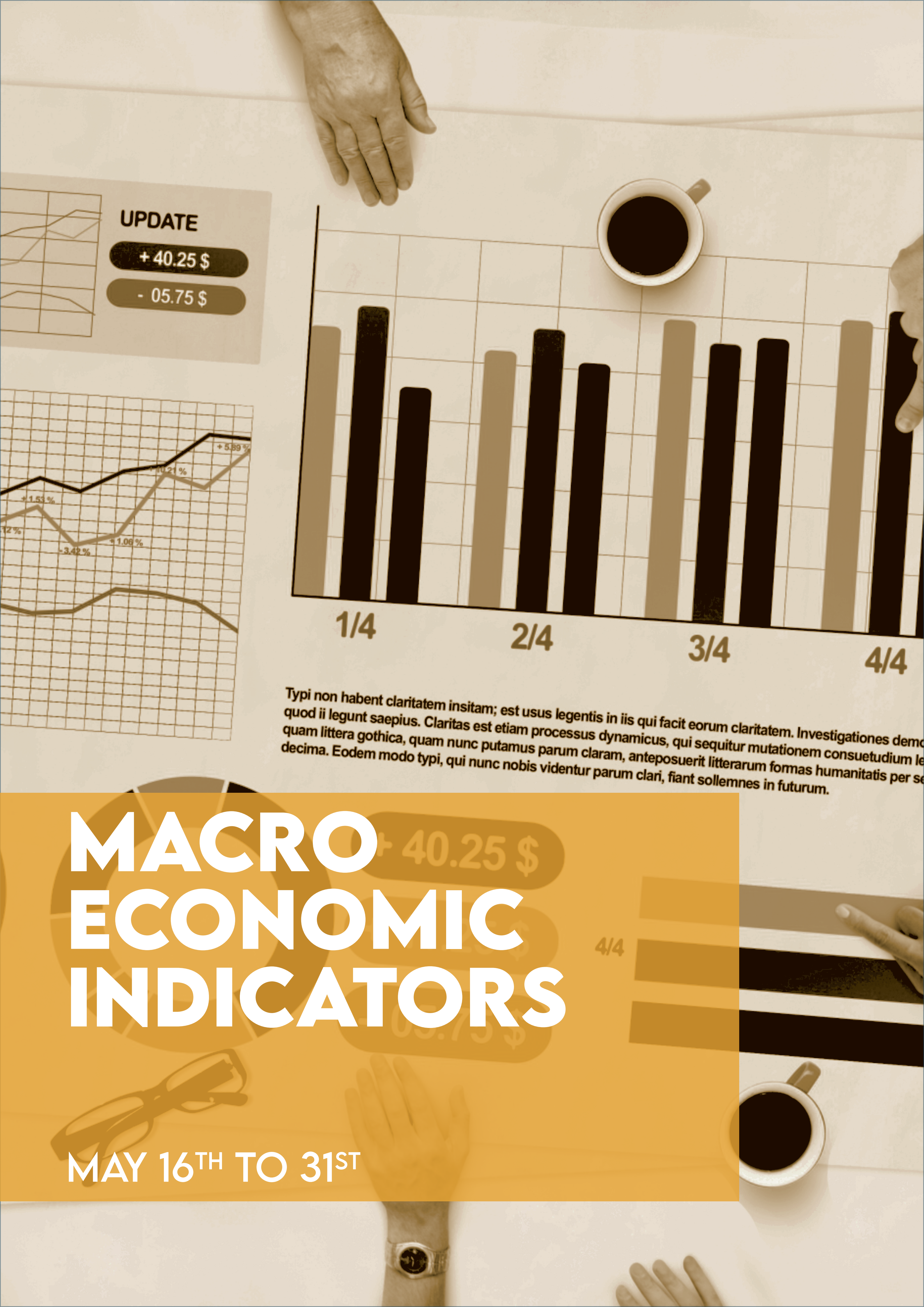


MACRO ECONOMIC INDICATORS

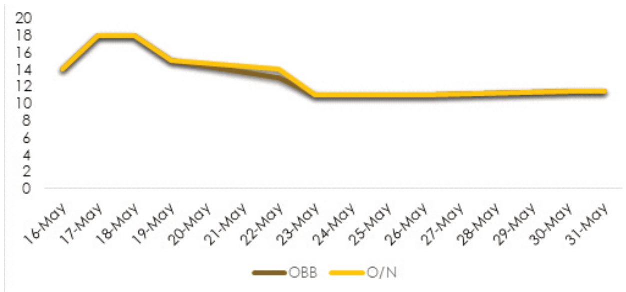
MAY 16TH TO 31ST

MONEY MARKET

The average opening position of banks was N196.02bn long in the second half of May. This is 159% higher than the average of N75.68bn short in the corresponding period in April. The boost in liquidity was partly due to OMO repayment of N10bn and primary market T/bill auction of N180.43bn. There were no OMO sales during the review period. The resulting impact of the spike in liquidity was a sharp drop in short-term interbank interest rates. Average NIBOR rates (OPR, O/N) declined by 215bps to 13.22%p.a. in the second half of May from 15.37% p.a. in the corresponding period in April.

In the second half of May, one primary market t/bill auction was conducted. A total of N180.43bn was allotted, which is 37.25% higher than the sum of N131.46bn allotted in the second half of April. T/bill yields fell across all tenors by an average of 155bps. Similarly, t/bill rates fell by an average of 87bps at the secondary market.

SHORT-TERM INTERBANK RATE (%)



Source: FDC Think Tank

Tenor	Primary market (May 10th 2023) (%)	Primary market (May 24th 2023) (%)	Secondary market (May 15th 2023) (%)	Secondary market (May 31st 2023) (%)
91-day	4.5	2.29 ▼	6.15	5.09 ▼
182-day	6.44	4.99 ▼	7.55	6.29 ▼
364-day	8.99	7.99 ▼	7.61	7.31 ▼

Source: FMDQ, FDC Think Tank

▲ 159%

N196.02BN

AVERAGE BANK OPENING POSITION

OUTLOOK AND IMPLICATION

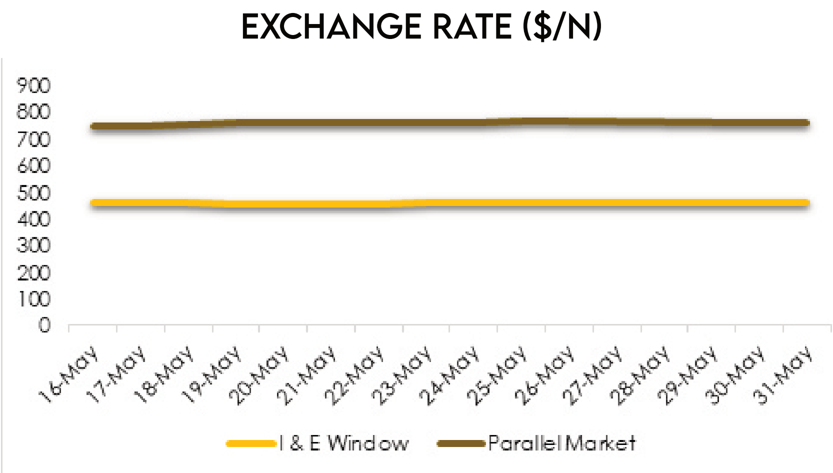
Short-term interbank rates are expected to remain at current levels pending a significant injection or withdrawal from the system.

FOREX MARKET

The forex market is currently being reformed. Recently, the CBN adopted a "willing-buyer-willing-seller" model thereby scrapping the multiple exchange rate system. Henceforth, the exchange rate will be determined by the forces of demand and supply. Some of the exchange rate determinants are balance of payments, capital inflows, and trade balance.

EXCHANGE RATE

At the Investors and Exporters Foreign Exchange window, the naira depreciated slightly against the dollar to close at N464.5/$ on May 31 from N464/$ on May 16. Whereas, at the parallel market, demand pressure increased amidst limited forex supply. This led to a depreciation (1.33%) in the value of the currency to N760/$ on May 31 from N750/$ at the start of the review period (May 16). As at today (June 15), the CBN appears to have liberalized the market and it is likely that the exchange rate will trade between N700/$ and N750/$ at all markets. Today (June 15), the parallel traded at N751/$.



Source: FDC Think Tank

▼ 1.33%

N760/$

PARALLEL MARKET RATE

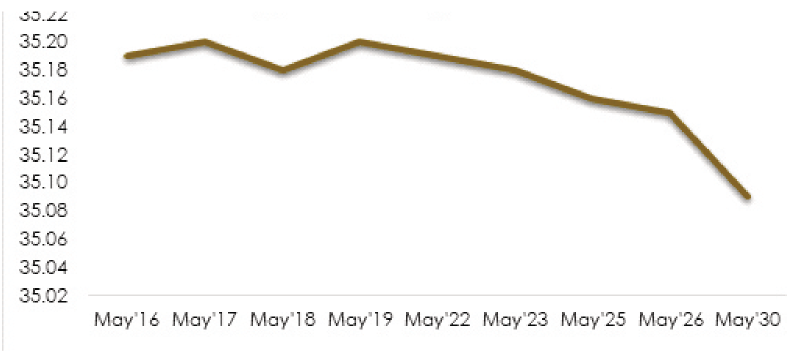
OUTLOOK

The external reserve is likely to continue its steady depletion in the near term as major sources of dollar inflows dwindle. However, the recent fuel subsidy removal is expected to aid external reserve accretion in the long run. Also, exchange rate unification implies that the naira would be traded at the market-clearing rate. Given that the purchasing power parity (PPP) of the naira is estimated at N684/$ and the parallel market rate is about N755/$ (as at June 15), it is expected that the unified rate could range between N700/$ and N755/$.

EXTERNAL RESERVES

In the second half of May, Nigeria's Foreign exchange reserves maintained its downward trajectory. It fell by 0.28% to close the month at $35.09bn on May 31st from $35.19bn at the beginning of the period. This was as oil price declined by 1.82% to $73.54pb from $74.91pb on May 16th. The country's import and payments cover decreased slightly by 0.37% to 7.96 months from 7.99 months on May 16th. So far in June (as at June 15), the external reserve has declined further to $34.81 billion.

FOREIGN EXCHANGE RESERVES



Source: CBN, FDC Think Tank

▼ 0.28%

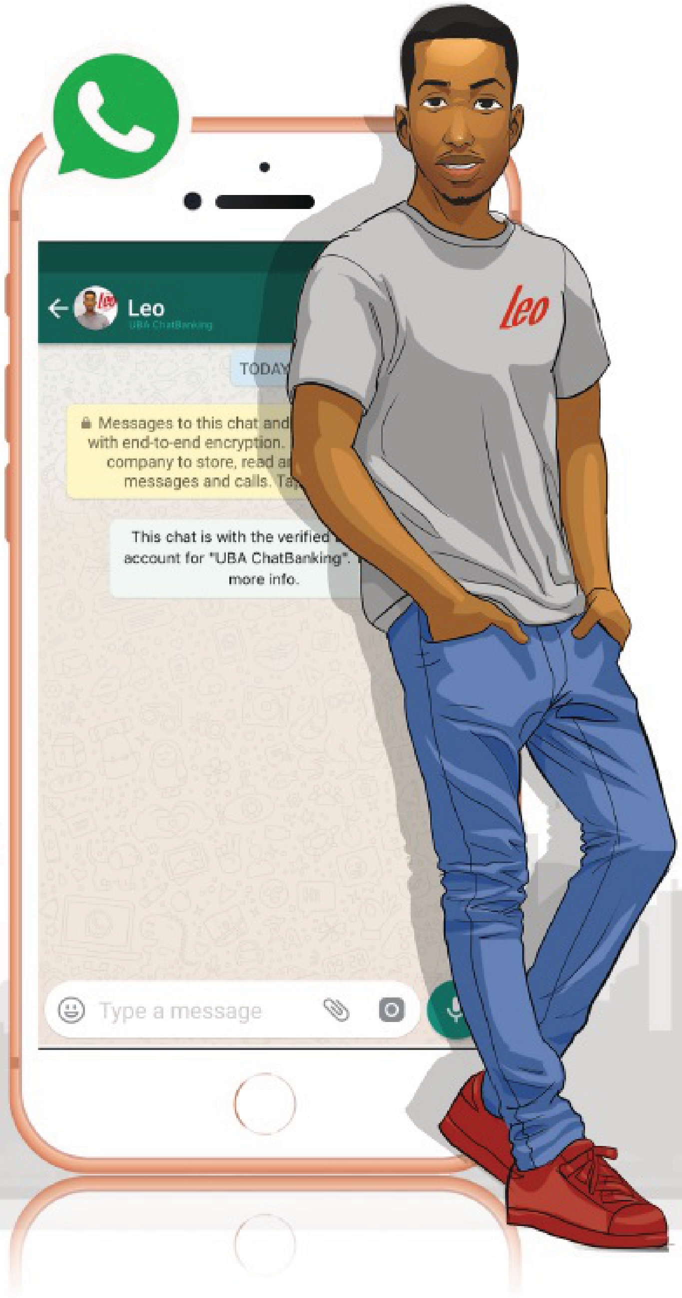
$35.09BN

NIGERIA'S EXTERNAL RESERVES

IMPLICATION

The further depletion of the reserves will limit the CBN's ability to intervene in the forex market, which could lead to Naira depreciation. It could also worsen the country's external imbalance and affect investor confidence owing to concerns over the country's ability to meet its obligations. Moreso, exchange rate unification could lead to squeeze in liquidity, resulting in increase in the effective interest rate.

UBA
United Bank for Africa



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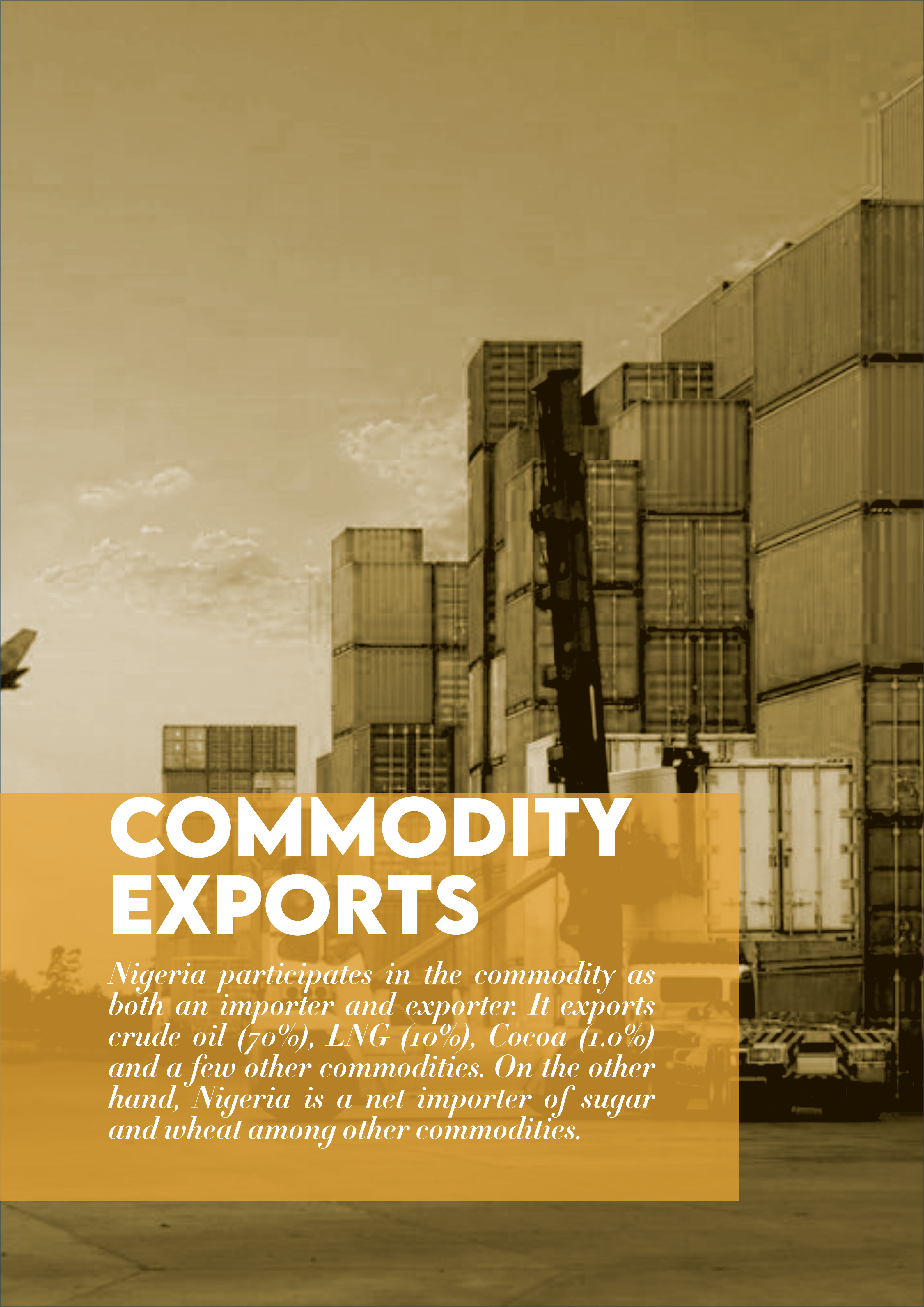


COMMODITY EXPORTS

Nigeria participates in the commodity as both an importer and exporter. It exports crude oil (70%), LNG (10%), Cocoa (1.0%) and a few other commodities. On the other hand, Nigeria is a net importer of sugar and wheat among other commodities.

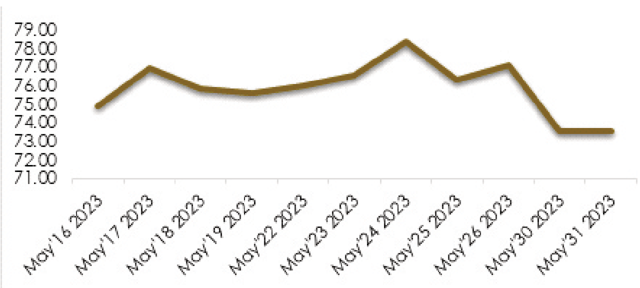
OIL PRICES

The price of Brent crude traded lower in the second half of May compared to the same period in April. It traded within the range of \$73.54/pb - \$78.36/pb. On average, oil prices decreased by 7.14% to \$75.88/bp from \$81.72/bp in the second half of April. The bearish market sentiment was bookended by weak Chinese economic data and increased US stockpile.

OIL PRODUCTION

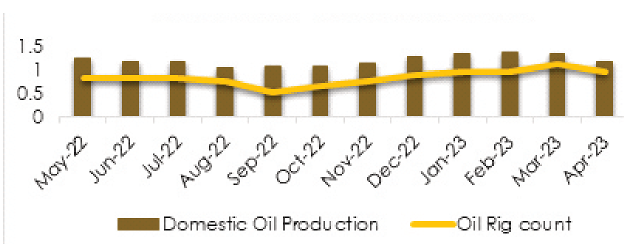
In April, domestic oil production fell further by 12.6% (170,000mbpd) to 1.18 million barrels per day from 1.35 million barrels per day in March. This was as the country's oil rig count fell by two points to 13 in April from 15 in March. OPEC's crude oil production fell by 191,000 barrels per day in April 2023, to an average of 28.6 million barrels per day when compared to 28.8 million barrel per day in March. Oil production increased in Saudi Arabia, Iran and Angola, while it declined in Nigeria and Iraq.

BRENT CRUDE OIL ($/PB)



Source: Bloomberg, FDC Think Tank

DOMESTIC OIL PRODUCTION



Source: OPEC, FDC Think Tank

▼ 12.6%

1.18mbpd

DOMESTIC OIL PRODUCTION

OUTLOOK

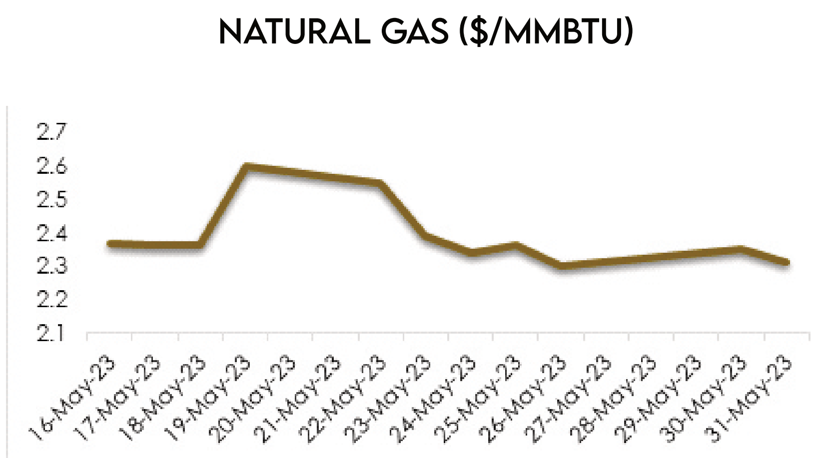
Oil prices are expected to decline in the near term owing to weakening demand from China and increased Russian supply exceeding Saudi Arabia's plans for further production cuts contributed to the decline. In May, Russia's supply to China and India reached record levels and it is expected to maintain the momentum.

IMPACT

The fall in oil price will lower the country's oil revenue and limit its foreign exchange earnings. As a result, FAAC allocation to the three tiers of government will shrink and could raise government borrowings in the capital market, pushing up its debt burden. Lower forex earnings would also affect the ability of the CBN to defend the Naira.

NATURAL GAS

In the second half of May, the price of gas fell marginally by 2.11% from $2.37/mmbtu to $2.32/mmbtu on May 31st. This decline was due to weak industrial demand as the technical recession in Germany weighed on the prospect of demand for natural gas. Gas price averaged $2.39/mmbtu within the review period (May 16th to 31st), up 3.9% from the average of $2.3/mmbtu in the second half in April.



Source: Bloomberg, FDC Think Tank

▲ 3.90%

$2.39/MMBtu

AVG NATURAL GAS PRICE

OUTLOOK

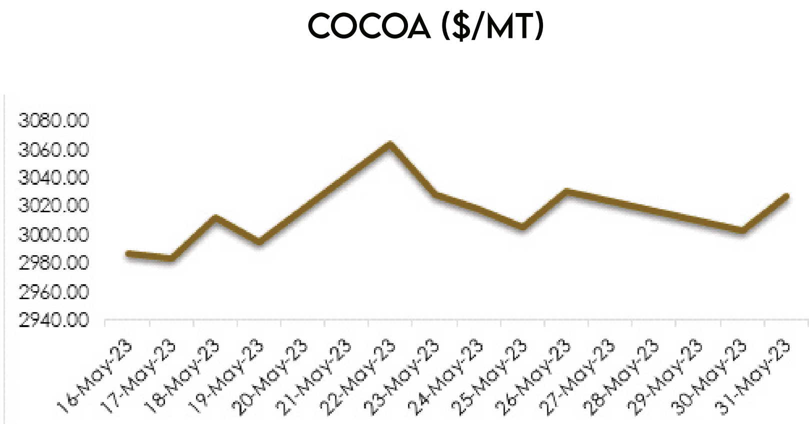
The price of gas is expected to remain low owing to rising stockpiles and subdued demand in Europe.

IMPLICATION

Gas accounts for 10.4% of total exports. Hence, low gas prices will dampen the country's external and fiscal revenues. However, this could lessen inflationary pressures for consumers and manufacturers who utilize gas.

COCOA

Cocoa prices fluctuated during the review period. It touched a high of $3,064/mt on May 22nd before losing ground to close at $3,027/mt on May 31st. The price of cocoa averaged $3,014/mt in the second half of May, up 2.34% from the average of $2,945/mt in the preceding month. This increase was buoyed by looming EU legislation bans that threaten supply amid supply concerns in key producing countries in West Africa.



Source: Bloomberg, FDC Think Tank

▲ 2.34%

$3014/mt

AVG COCOA PRICE

OUTLOOK

Cocoa price is likely to increase in the near term owing to supply tightness in top producer, Ivory Coast.

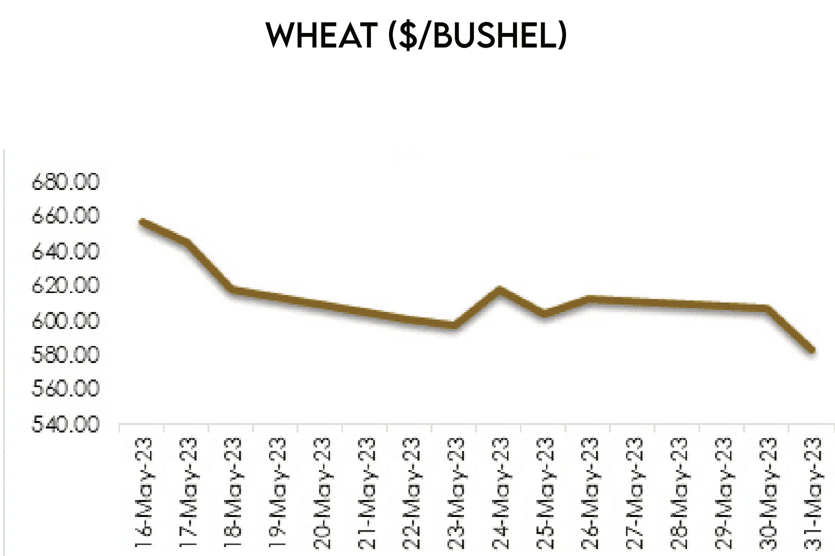
IMPLICATION

Cocoa is a major non-oil export commodity in Nigeria. A rise in cocoa prices will boost the country's foreign exchange earnings as well as government revenue. This will also increase the income of cocoa farmers.

COMMODITY IMPORTS

WHEAT

The price of wheat fell significantly in the second half of May mainly as supply concerns eased due to favorable weather condition in North America amid the extension of the black sea export deal. It declined by 11.19%, to close the period at $583.25/bushel from $656.75/bushel on May 16th. On average, wheat prices fell to $614.18/bushel within the review period from the average of $664.12/bushel in the second half of April.



Source: Bloomberg, FDC Think Tank

▼ 7.52%

$614.18/b

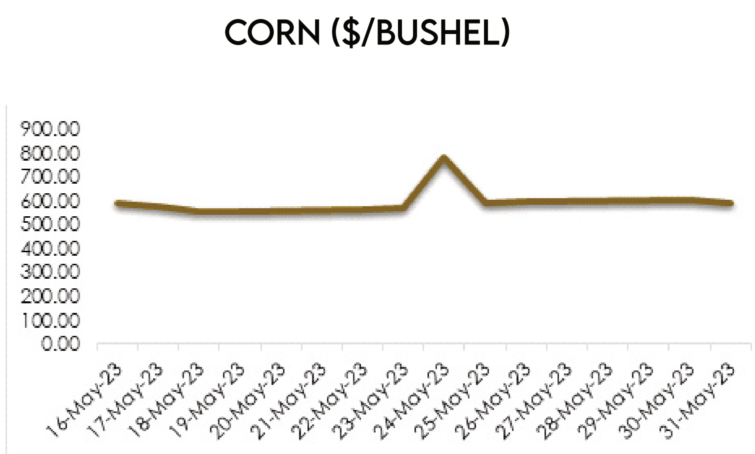
AVG WHEAT PRICE

OUTLOOK- GRAINS

The price of wheat is likely to fall on expectations of ample production in key exporting countries which could weigh in on prices. Similarly, corn prices are expected to trend downwards owing to slowing demand for US supplies.

CORN

In the second half of May, corn price was relatively stable. It touched a high of $782.5/bushel on May 24th despite export increases in USA, a top corn producer, before gaining momentum to close the period at $589/bushel. On average, the price of corn fell by 7.10% to $596.27/bushel in the second half of May from $641.88/bushel in the same period in April spurred by increased global supply.



Source: Bloomberg, FDC Think Tank

▼ 7.10%

$596.27/b

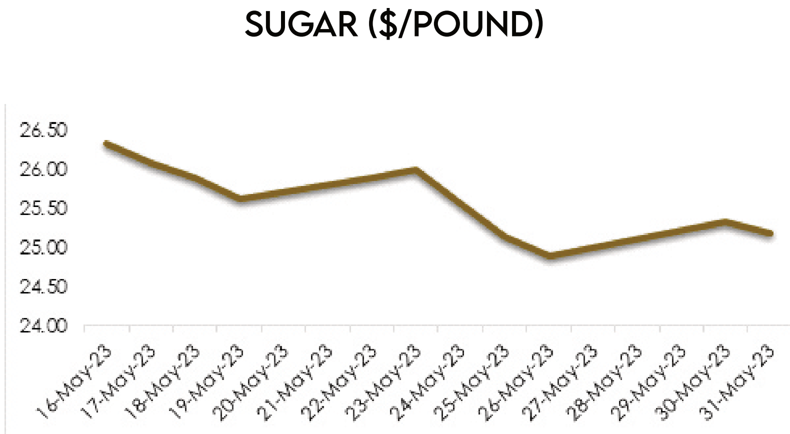
AVG CORN PRICE

IMPLICATION - GRAINS

Lower grain prices are expected to reduce the country's import bill as well as the manufacturing cost for food processing companies. This reduces the danger of inflation as retail prices fall, resulting in a gain in consumers' real income.

SUGAR

The price of sugar trended downward in the second half of May. It fell by 4.33% to close the period at $25.18/pound from $26.32/ pound on May 16th. This decline was driven by projections of improved supply from Brazil alongside progress in Indian sugar production. Overall, sugar prices averaged $25.63/pound in the second half of May, 2.27% higher than the average of $25.06/ pound in the same period in April.



Source: Bloomberg, FDC Think Tank

▲ 2.27%

$25.63/lb

AVG SUGAR PRICE

OUTLOOK

The price of sugar is expected to remain low in the near term as major exporter Brazil records a bumper harvest for the next crop season.

IMPLICATION

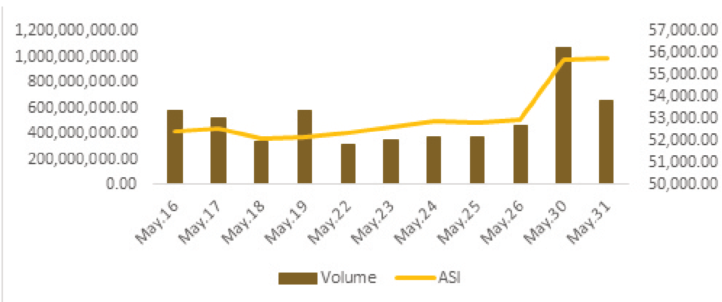
Low sugar price will ease pressure on the foreign exchange reserves as import bill reduces.

STOCK MARKET REVIEW

MAY 16TH TO 31ST

Nigerian Exchange Limited closed on a positive note from May 16th-31st. It gained 6.77% to close at 55,769.28 basis points on May 31st, up from 52,231.09 basis points on May 15th. Also, the market capitalization increased by 6.78% to N30.37 trillion (trn) relative to its close of N28.44 trillion (trn) on May 15th. The market YTD return rose to 8.82% from 1.91% in the preceding period. The market breadth was positive at 5.19x as 83 stocks gained, 57 stocks remained unchanged while 16 lost. The positive performance of the NGX could be partly attributed to renewed market sentiment as investors began to position themselves for possible opportunities and reforms from the new administration. So far in June (June 14), the market YTD return is 17.04%. The current rally is being fueled by the suspension of the former CBN governor, Mr. Emefiele, and the expectation that the government will unify the exchange rate.

NGX PERFORMANCE



Source: NGX, FDC Think Tank

The market activity level was mixed in the review period. The average volume traded decreased by 21.92% to 513.15mn units from 657.38mn units. Meanwhile, the average value of trades rose by 58.95% to N8.79bn from N5.53bn in the review period.

The performance of the sectors was positive in the review period, as all five sectors gained.

SECTOR PERFORMANCE

Industrial	FMCG	Banking	Oil &Gas	Insurance
5.09%	14.13%	14.72%	7.34%	10.22%

TOP 5 GAINERS

FTN Cocoa Processors Plc topped the gainers' list with a 161.29% increase in its share price. This was followed by Chams Plc (63.33%), Tripple Gee & Co Plc (44.44 %), Ikeja Hotel Plc (38.60%) and RT Briscoe Nigeria Plc (37.04%).

TOP 5 LOSERS

The laggards were led by Ardova Plc (-34.47%), Consolidated Hallmark Insurance Plc (-21.21%), Chellarams Plc (-18.78%), Sovereign Trust Insurance Plc (-14.29%) and Computer Warehouse Group Plc (-10.16%).

Company	May- 15 (N)	May- 31 (N)	Absolute Change	Change (%)
FTNCOCOA	0.31	0.81	0.50	161.29
CHAMS	0.30	0.49	0.19	63.33
TRIPPLEG	2.70	3.90	1.20	44.44
IKEJAHOTEL	1.71	2.37	0.66	38.60
RTBRISCOE	0.27	0.37	0.10	37.04

Company	May- 15 (N)	May- 31 (N)	Absolute Change	Change (%)
ARDOVA	26.40	17.30	-9.10	-34.47
CHIPLC	0.66	0.52	-0.14	-21.21
CHELLARAM	1.81	1.47	-0.34	-18.78
SOVRENINS	0.42	0.36	-0.06	-14.29
CWG	1.87	1.68	-0.19	-10.16

OUTLOOK

We expect investors to continue to take positions in oil and gas downstream, telecommunications stocks, who are major beneficiaries of the fuel subsidy removal. The expectation that the government will sustain its reform agenda, especially in the forex market, will continue to support a bullish market in the near term.

OUTLOOK FOR NEXT MONTH

Nigeria is currently undergoing a series of reforms, including subsidy removal, exchange rate adjustment, power sector reforms, and "housecleaning" of critical institutions. In the coming days, it is expected that other reforms such as debt restructuring, the justice system, and tax reforms will follow. Most markets, including the equities and bond markets, have responded positively to the reform grenades; this is an indication of an improvement in investor confidence. Following the exchange adjustments and the subsidy removal, it is expected that FAAC allocation will improve in the coming months. The increased transparency in the forex market could bolster invisible inflows as well as foreign investment inflows. This could strengthen the naira in the near term. Our model, however, shows that the subsidy removal could push up prices by 3% to 25.2% in June.