

Macro Economic Report | Monthly Update

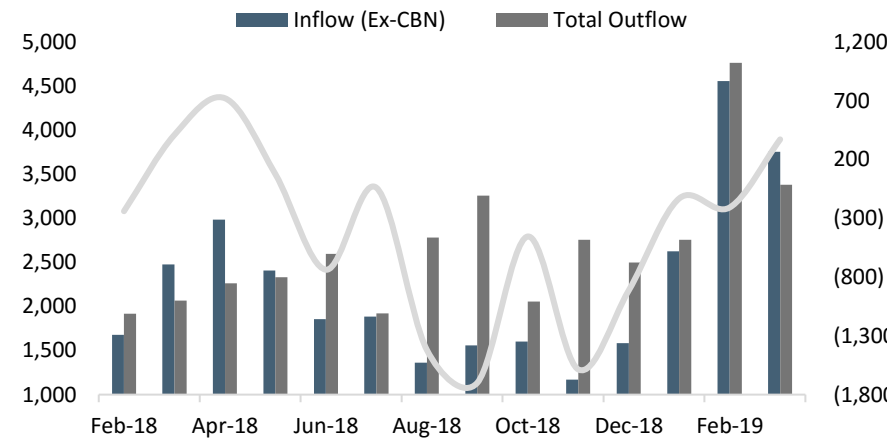
Macro Economic Update – March 2019

A more compelling story for FX stability

The balance of flows at the Investors and Exporters Window (IEW) turned to a positive of \$372 million in the month of March, from a net outflow of \$208 million in February. The surplus at the IEW (ex-CBN) emanated largely from faster decline in outflows compared to inflows. Going by breakdown, FPI flows declined 22% MoM to \$2.7 billion (\$3.5 billion in February) to account for 94% of total offshore funds. On the local leg, dollar supply (ex-CBN) rose slightly by 7.6% MoM to \$870 million, with cumulative total flows ex-CBN settling at \$3.7 billion (-17.6% MoM). Elsewhere, outflows at the window moderated faster in the month by 29% MoM to \$3.4 billion. As a result, reported net purchase by the apex bank during the month stood at \$1.4 billion. Reflecting the net inflow at the IEW and increased oil inflows induced by higher crude oil prices and production, the gross external reserves recorded the first monthly accretion in the year of \$2.1 billion to \$44.4 billion with import cover spanning ~15 months.

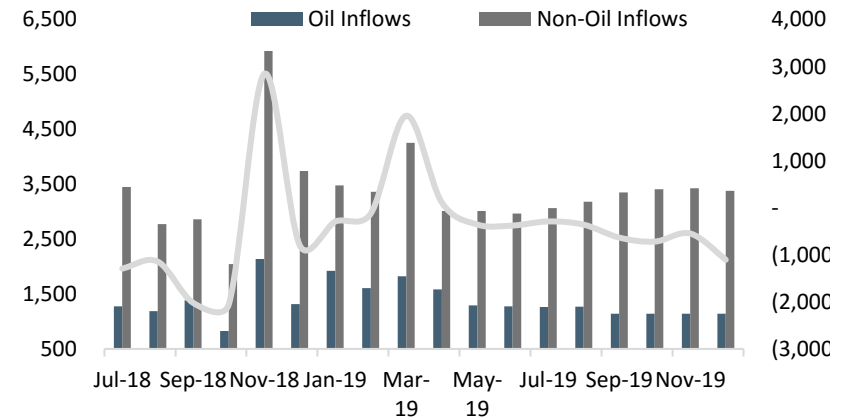
While we have no official data to back this claim, recent flows of funds and the activities in the fixed income market suggests most of the offshore flows were propelled by the clear sign of further moderation in yields on treasury assets and likely disappearance of attractive carry-trade in the months ahead. While we maintain our thesis of near-term FX stability, lower fixed income maturity (with foreign investors holding ~36% of total FI holdings) suggests lower pressure on the reserves and a more stable FX over the rest of the year. Coalescing our modeled inflow to the CBN of \$51.1 billion and outflow of \$53.5 billion, we expect average monthly reserve drawdown of \$223 million over 2019, suggesting cumulative \$2.5 billion depletion in the reserve to \$40.1 billion (excl. proposed Eurobond of \$2.7 billion).

Figure 1: Foreign Currency flows through the IEW (\$'bn)



Source: FMDQ, ARM Research

Figure 2: Foreign Currency flows through the CBN (\$'Billion)



Source: FMDQ, ARM Research

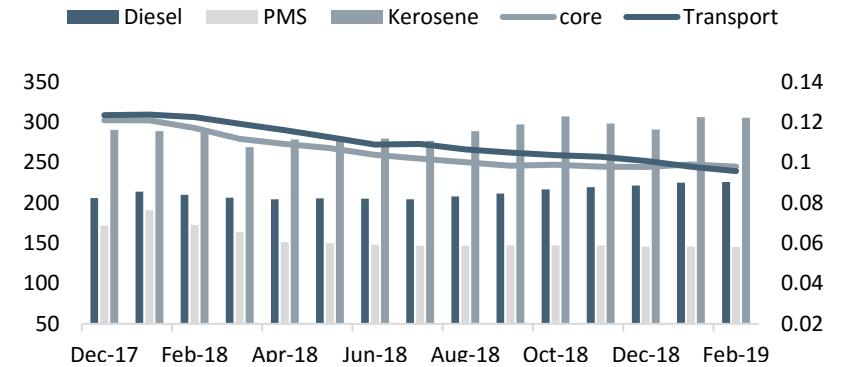
No risk to inflation in the near term

With continuity being the theme for this year and the undertone observed within the current government, we update our views on risk to consumer prices and cut our average inflation rate over 2019 to 10.6%. For clarity, while the case for a PMS hike this year seems justified, our interactions with oil marketers and government officials reveals the current regime is very reluctant to make an upward review to PMS price from current ₦145/litre.

Inflation rate for the month of February dipped to 11.31%, down from 11.37% recorded in the prior month, following moderation in both the food and core indices. On a Month on Month basis, headline inflation dipped by 1bps to 0.73%, following a faster decline in core inflation by 15bps MoM to 0.65%. Notably, the declines were evident across major sub-indices - transport (-3ps), health (-3bps), clothing (-2bps), furnishing (-3bps), while the HWEGF rose 2bps. Food on the other hand only dipped by 1bps to 0.82% stemming from a decline in processed food (-171bps to 0.82%), as farm produce ticked up in the month (+15bps to 0.82%).

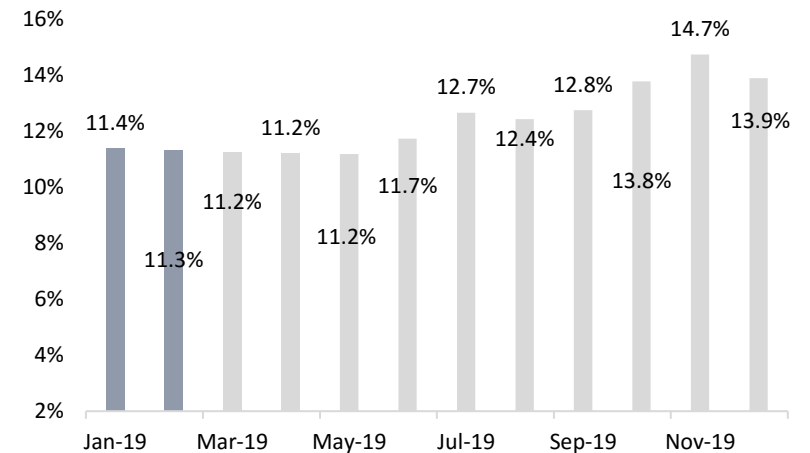
For the month of March, we expect further decline in inflation to 11.25% YoY as both core and food inflation firmed further. While we still expect diesel and kerosene prices to remain elevated relative to the prior month, lower PMS prices (-11% YoY) guides our view of a further moderation in core inflation. Likewise, with dry season and cassava harvest expected during the month, we see further moderation in food inflation compared to the prior year. According to FEWSNET, staple prices have either been stable or declined slightly relative to the prior year, however, prices of both imported and local rice are expected to rise similar to the trend observed in February. That said, we might start to see slight pressure on MoM food inflation in march. Overall, with no shocks to inflation in view, we expect inflation rate to touch single digit towards the end of the year with full year estimate at 10.6% YoY (FY 18: 12.2% YoY).

Figure 3: Avg. energy prices (₦/litre) vs. Core & Transport Inflation (% YoY)



Source: NBS, ARM Research

Figure 4: Inflation rate – Actual and Forecast (YoY)



Source: NBS, ARM Research

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