

Economic Report | Inflation
Inflation: A temporary pause on a downward trend
Economic Snapshot

October Inflation Data/Indices			
	MoM	YoY	Prev YoY
Headline	0.76%	15.9%	16.0%
Food	0.84%	20.3%	20.3%
All Items Less Farm	0.77%	12.1%	12.1%
Imported food	1.28%	15.3%	14.9%
Energy	0.70%	9.86%	9.74%
Currency Markets			
	Latest	Daily Chg	YTD
USDNGN	359.9	0.00%	14.2%
EURNGN	423.4	-0.40%	27.7%
GBPNGN	477.6	0.25%	22.1%
JPYNGN	321.0	-0.31%	19.3%
Monetary Aggregates – August 2017			
	(₦bn)	MoM	YoY
M2	21,851	-1.6%	-0.9%
CPS	21,997	-0.8%	-3.6%
NCG	4,824	-17.8%	35.9%
NFA	9,733	11.3%	32.4%
NDC	26,821	-4.3%	1.8%
External Position			
	Latest	QoQ	YoY
Trade Balance (\$'mn)	84.8	-9.6%	N/A
External Reserves (\$'mn)	34,356	8.89%	41.77%
Foreign Debt (\$'mn)	15,352	2.03%	32.55%
Growth Data – Q3 2017			
	(₦bn)	%of total	YoY
Real GDP	17,800	100%	1.4%
Agriculture	5,189	29.2%	3.1%
Oil	1,788	10.0%	25.9%
Services	5,765	32.4%	-3.1%
Wholesale and Trade	2,829	15.9%	-1.7%
Manufacturing	1,569	8.8%	-2.9%

Amaka Ukoha

amaka.ukoha@arm.com.ng

In the month of October, Nigeria's consumer price index sustained its moderation, to a 17-month low of 15.91% YoY, as modest gains from food offset a slight increase in the core basket. The latter increased by an annual rate of 12.14%, 2bps higher than September's reading, largely underpinned by subsisting inflationary pressures across energy, processed food, restaurants, and furnishings & household equipment maintenance divisions. Elsewhere, while food inflation attuned to the impact of harvest season on food prices, the scale of moderation expected was capped by pressures in processed food and imported food segments. Consequently, food inflation moderated slightly by 1ppt to an annual rate of 20.31%.

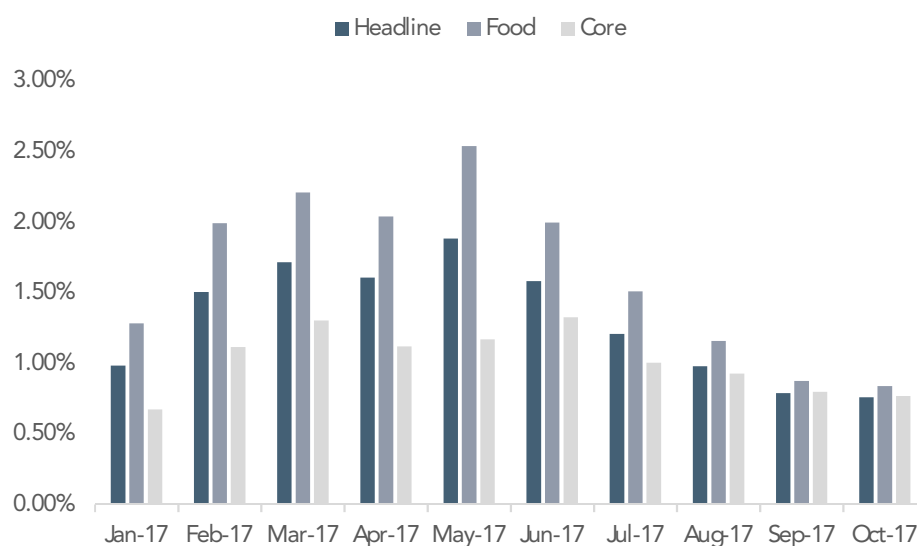
Soft Headline, but MoM is firming

Month-on-month (MoM) inflation was more reflective of the underlying price pressure. After moderating by an average of 27bps in the last four months, MoM inflation declined by 3bps in the month of October to 0.76%, largely reflecting price pressure at both sub-components. Specifically, while MoM food inflation came in lower at 0.85% relative to prior months' reading (0.87%), the reading tracked slightly ahead of our prior five-year October mean of 0.71%¹.

¹ October is mainly characterized by harvest-induced slowdown in food prices

Precisely, we had expected pressures on the food basket to moderate sizably as the harvest season reaches its peak in October as well as continued benefits from the lagged impact of energy gains which should have tapered transport inflation². However, despite the peak of the harvest season in October, farm produce inflation of 0.75% MoM³ and processed food of 1.79% MoM contracted modestly relative to the prior month (Farm produce: 0.75% MoM, Processed foods: 1.79% MoM). Similarly, transport inflation remained elevated at 0.78% MoM (September: 0.8% MoM) relative to our forecast of 0.72% MoM reflecting the impact of higher energy prices (+5bps to 0.70% MoM largely due to an increase in diesel prices⁴ (+9.28% MoM). Furthermore, NBS commentary revealed that prices of maintenance, repairs, vehicle spare parts and other services related to transport equipment increased sharply in October which in our view likely exacerbated pressures on transport inflation. On a positive note, imported food inflation contracted (-3bps to 1.28% MoM) reflecting gains from sustained FX liquidity.

Figure 1: MoM core and food inflation vs. headline MoM (Jan – Oct 2017)



Source: NBS, ARM Research

² Lower transport inflation forecast was hinged on sustained gains from the lagged impact of lower energy prices

³ NBS noted increases in the price of bread and cereals, meats, oils and fats, coffee, tea and cocoa, milk, cheese, eggs, vegetables, and fish.

⁴ In October, Major Oil Marketers Association of Nigeria (MOMAN) increased diesel prices to a range of N210-N225 from an average of N160-N190 between July to September to capture the impact of higher global crude oil prices in a deregulated market.

Downtrend in core inflation short-lived as pressures resurface

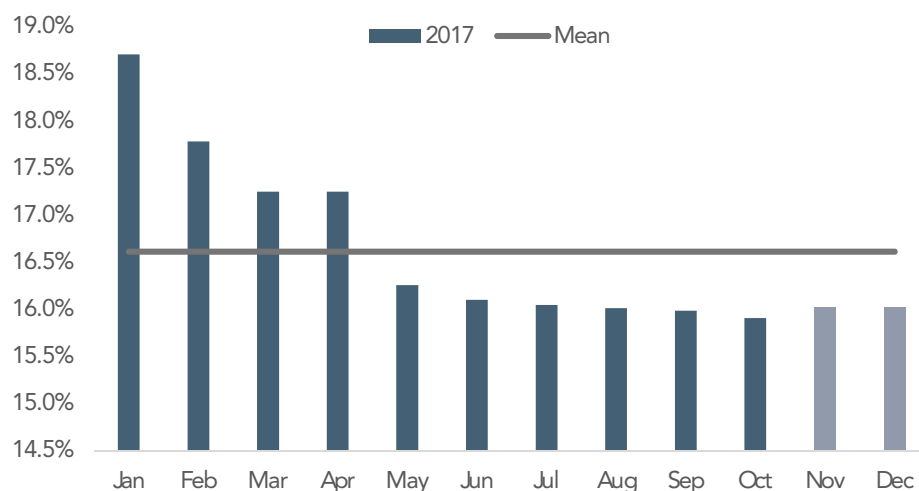
October's MoM core reading came in at 0.77%, its lowest level in eight months. From breakdowns provided, the temperance in the core basket reflects the impact of declines in education (-92bps), HWEGF (-31bps), alcoholic beverage, tobacco, and kola (-19 bps), clothing and footwear (-18bps) and communication (-13bps) divisions. These gains offset the inflationary pressures across processed food (+184bps), restaurants (+41bps), furnishings & household equipment maintenance (+20bps), health (+13bps), transport(+16bps), and miscellaneous goods (+20bps). Notwithstanding the subdued MoM reading, YoY core inflation accelerated in October (+2bps to 12.14% YoY), after a brief respite in the prior month.

Subsisting food pressures underpin bleak outlook for inflation

Given the conclusion of the main harvest in October, we now expect firming MoM headline inflation to be evident in the month of November underpinned by an uptick in food inflation which should offset gains from subdued core inflation reading. Our expectation for elevated MoM food inflation is largely reflective of sticky transport inflation underpinned by higher diesel prices as well as ramp-up in the demand for cereals and other food produce against the imminent approach of the December festive period.

On the core front however, we expect MoM reading to sustain its decelerating trend in November as gains from monthly sustained FX liquidity persists and against the backdrop of fading supply shocks. On balance, we now look for MoM headline inflation reading of 0.88% in November 2017 with the implied YoY reading expected to come in at 16% YoY. In December, we expect MoM headline inflation to remain elevated and dictated by inflationary pressures on the food index –a fallout of the festive Christmas period while sustained FX liquidity underpins MoM core inflation at subdued levels. Overall, we look for December and 2017 mean YoY headline inflation of 16% and 16.61% respectively.

Figure 2: YoY Inflation (Jan – Dec 2017) vs. 2017 expected average



Source: NBS, ARM Research

Absence of near term supply shocks to drive benign inflation over 2018

As iterated in our prior reports, we see little scope for substantial shocks on headline inflation in 2018. Precisely, against the 2019 elections and what looks set to be, a tough electioneering campaign, we expect PMS and electricity prices to remain relatively stable. Against these backdrop, we see scope for substantial deceleration in headline inflation in 2018 owing largely to high base effects from 2017 with headline inflation projected to average 13.3% over H1 18. Consequently, we expect that the argument in favour of elevated rates to keep real return positive to lose steam over H1 18 owing to high base effect and the absence of significant price shock which should ease the scope of inflationary pressures on headline inflation.

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