



July 2023 CPI Report: Removal of PMS Subsidy & FX Liberalization Bites Hard

Headline Inflation Spikes to 24.08% YoY in July 2023

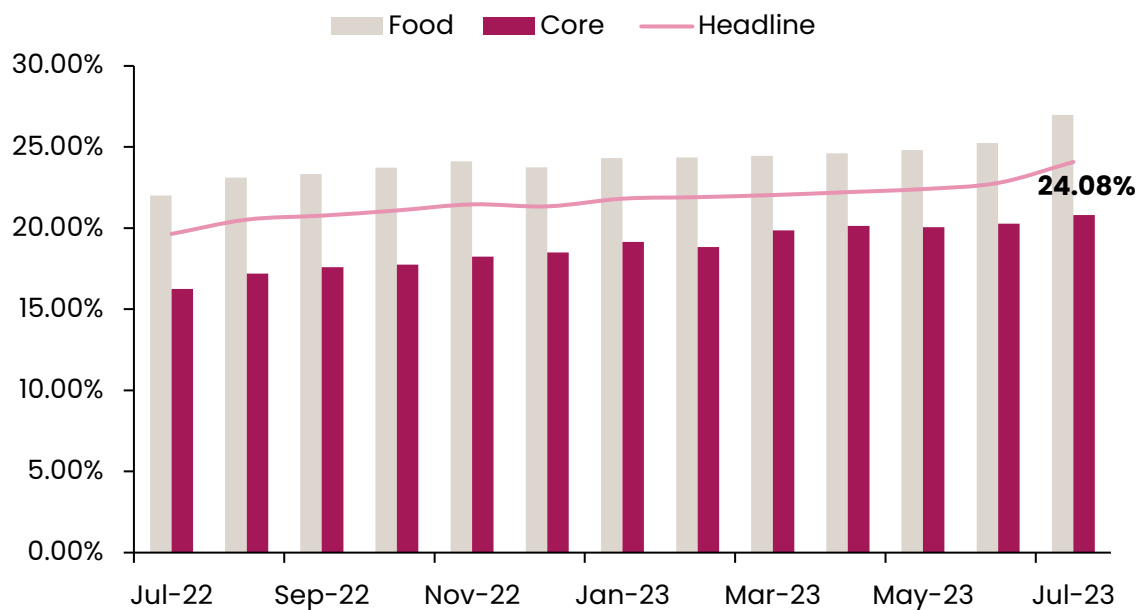
Earlier this week, the NBS¹ released the inflation report for July 2023. Headline inflation spiked by 129bps YoY² to 24.08% (vs 22.79% in June 2023), marking the highest rate recorded in Nigeria since the reconstitution of the CPI³ in 2009. The surge in Headline inflation is on the back of a jump in Food inflation (+173bps YoY to 26.98%) and Core inflation (+41bps YoY to 20.47%). It is however noteworthy, that after the removal of Premium Motor Spirit (PMS) subsidy and the resulting volatility in energy prices, the NBS has changed its definition of Core inflation from 'All items less farm produces' to 'All items less farm produces and energy'. Consequently, Energy inflation noted an uptick of 90bps YoY to 21.91% (vs 21.00% in June 2023). On Month-on-Month (MoM) basis, Headline inflation displayed similar trajectory as it advanced by 76bps to settle at 2.89% (vs. 2.13% in June 2023).

¹ National Bureau of Statistics

² Year-on-Year

³ Consumer Price Index

Figure 1: One Year Trend in Food, Core and Headline Inflation (%)



Source: NBS, ARM Research

Food Inflation: Incessant Pressure on Household Income

In July 2023, Food inflation climbed 173bps YoY to reach 26.98% compared to 25.25% in June 2023. This marks the seventh (7th) consecutive rise in Food inflation since its fall in December 2022. Notably, all its major sub-components, Farm produce (+188bps YoY to 26.60%), Processed food (+169bps YoY to 27.09%), and Imported food (+84bps YoY to 19.94%) recorded significant increases. We allude that the removal of PMS subsidy and further deterioration of the exchange rate contributed to the surge in food prices during the month. Furthermore, structural issues including insecurity, logistics challenges and poor storage facilities continue to be a bane to the stability of food prices. For the most part, Food inflation jumped to 3.45% MoM in July 2023 from 2.40% MoM in June 2023.

Core Inflation: New Measurement, Same Story

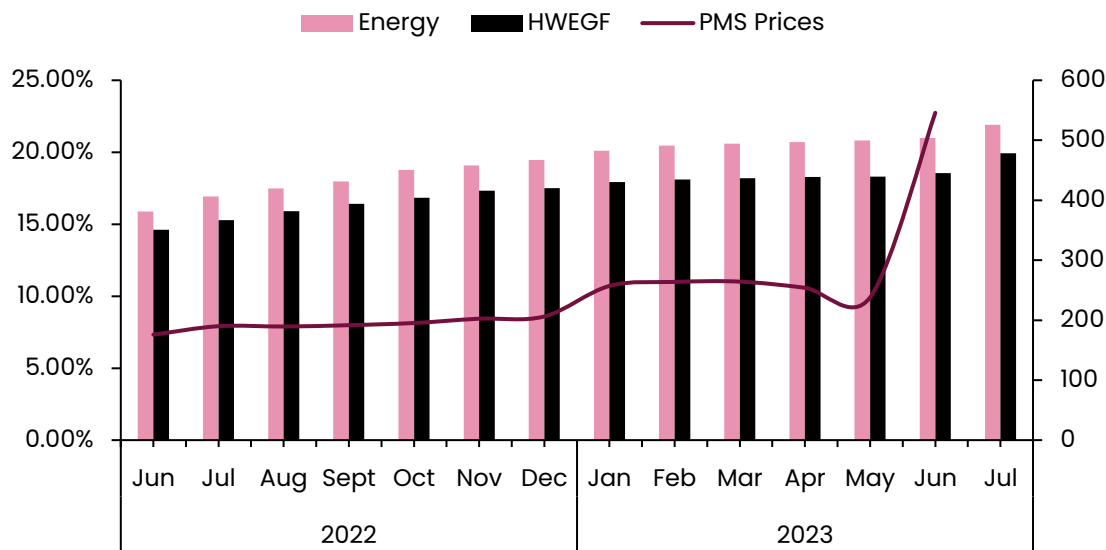
Following the recent volatility in energy prices after the elimination of fuel subsidy, energy has been excluded from the calculation of Core inflation. Consequently, Core inflation for June 2023 and previous months have been revised. In July 2023, Core inflation ticked up by 41bps YoY to 20.47% from 20.06% in June 2023 (June 2023 previous estimate: 20.27%). This is following significant increases in prices of Transport (+144bps YoY to 26.27%), Health (+71bps YoY to 21.84%) and Restaurant and Hotels (+120bps YoY 20.65%). We believe that the uptrend in fuel pump prices contributed to the significant rise in transport in July 2023. Overall, Core inflation went up by 34bps MoM to 2.11% (vs. 1.77% in June 2023).

Energy Inflation: Breaking New Ground

Energy inflation, which now stands alone after its exclusion from Core inflation, jumped by 90bps YoY to 21.91% in July 2023 (vs. 21.00% in June 2023). This represents the highest level since March 2017, when fuel prices rose following severe depreciation of the Naira. Consequently, HWEGF⁴ surged by 138bps YoY to 19.93% in July 2023 (vs. 18.55% in June 2023). Without doubt, the escalation in energy inflation is on the back of the removal of PMS subsidy. In addition, the FX liberalization policy played a major role in the surge in energy inflation, as cost of importing fuel has become elevated following the further depreciation of the Naira. On a MoM basis, Energy inflation increased by 84bps to 2.50% in July 2023 from 1.65% in June 2023. Similarly, HWEGF rose 99bps MoM to 2.60% (vs. 1.61% in June 2023).

⁴ Housing, Water, Gas and other Fuels

Figure 2: Trend Analysis of Energy Inflation, HWEGF and Average PMS Prices from June 2022 – July 2023



Source: NBS, ARM Research

Economic Activities Continue to Slip in July 2023

The PMI⁵ figure for July 2023 showed that economic activities extended their decline for the second (2nd) consecutive month since its rebound in May 2023. However, it remained above the 50.0 points benchmark (which indicates improved economic activities) for the fourth (4th) straight month. The PMI figure slipped from 53.2 points in June 2023 to 51.7 points in July 2023. We believe that the fall in the PMI figure for July 2023 is on the back of persistent inflationary pressures, which has driven cost of production to a new high. Furthermore, the rapid increase in petrol prices negatively affected economic and production activities during the period. In the coming months, we expect that rapid growth in price levels propelled by a depreciating Naira and increasing fuel prices will continue to hinder economic activities.

⁵ Purchasing Managers' Index

Outlook

We maintain that the sustained depreciation of the Naira against the dollar and rise in petrol prices will further exacerbate inflation, particularly food prices, transport prices and energy prices. Hence, barring government intervention in the downstream oil and gas sector and improvement in FX supply, we believe that inflation will continue its uptrend. Consequently, we expect higher inflation reading for August 2023.