NIGERIA | MACROECONOMIC UPDATE | INFLATION | INSIGHTS

FUNDAMENTALS

NIGERIA CPI UPDATE: A BITTER TASTE

27 APRIL 2023

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IN BRIEF

- Nigeria's headline inflation continued the upturn in March 2023, rising by 13bps to 22.0% y/y as higher food inflation left a bitter taste.

- On a month-on-month basis, price pressures were stronger with the sequential rate rising by 15bps to 1.9% m/m as the lingering FX volatility on the parallel market nudged the monthly food inflation above 2.0%.

- We attribute the rise in headline inflation to the persistent Naira depreciation on the parallel market and the structural bottlenecks with food production and domestic supply chains. In the near-term, we foresee continued upside risk to food inflation due to poor harvest following the severe flood in the agrarian states in 2022, continuing supply chain disruptions and incessant insecurity.

- As the main drivers of Nigeria's inflation are non-monetary, we believe that the Central Bank's monetary policy tightening will be less effective against the first-round effect of structurally-induced price shocks. However, we expect the Central Bank to continue signalling its commitment to price stability with another hike in the monetary policy rate, but at a slower pace than the previous increase in March 2023.

Food price pressures sustained the upward momentum in headline inflation

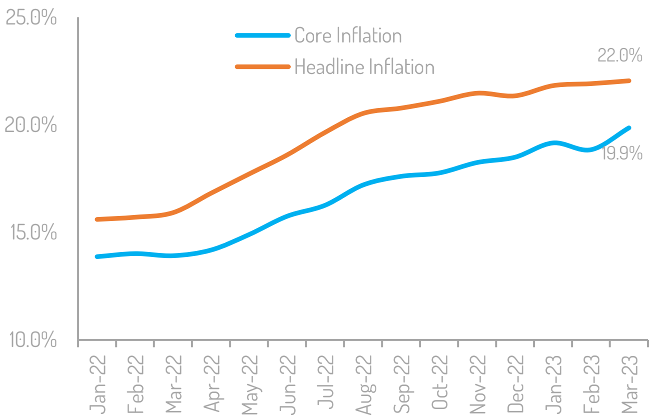
Nigeria's headline inflation continued the upturn in March 2023, rising by 13bps to 22.0% y/y as higher food inflation left a bitter taste. Inflation for food & non-alcoholic beverages climbed 10bps to 24.5% y/y, remaining above the headline rate by 250bps. Food inflation accounted for 11.4% of the headline inflation, exerting the highest influence on the overall price index.

Additionally, core inflation (that is, the overall CPI excluding food price index) edged up 10bps to 19.9% y/y. While we observed a gentle rise in headline inflation during 1Q2023, core inflation increased sharply over the same period. In our view, this underscores the stronger price pressures fuelled by the impact of the just-ended political season on aggregate demand and structural constraints to supply.

Although we expect the Central Bank's ongoing currency swap to tame Naira liquidity and cap the demand-side pressures, we equally foresee the associated worsening of domestic supply chains as an upside risk to inflation in the near term.

We attribute the rise in headline inflation to the persistent Naira depreciation on the parallel market and the structural bottlenecks with food production and domestic supply chains. Furthermore, we believe the rampant flooding across food production states in late 2022 remains a major driver of food inflation.

Core inflation vs headline inflation, Year-on change (%)



Source: National Bureau of Statistics

On a month-on-month basis, price pressures were stronger with the sequential rate rising by 15bps to 1.9% m/m as the lingering FX volatility on the parallel market nudged the monthly food inflation above 2.0%.

In the near-term, we foresee continued upside risk to food inflation due to poor harvest following the severe flood in the agrarian states, continuing supply chain disruptions and incessant insecurity. We also anticipate continued upside risk to core and headline inflation arising from higher energy prices which could heighten with the expected removal of fuel subsidy by Nigeria's new administration.

The Central Bank will continue its restrictive policy

At its March 2023 MPC meeting, the Central Bank (CBN) raised the monetary policy rate by 50 basis points to 18.0% with the aim to reverse the upward trend in inflation. The monetary policy committee considered that it would be better to remain cautious, due to the internal and external inflationary pressures facing the country's economy, including rising energy prices, continued pressure on the exchange rates, and unfavourable climatic conditions.

As the main drivers of Nigeria's inflation are non-monetary, we believe that the Central Bank's monetary policy tightening will be less effective against the first-round effect of structurally-induced price shocks. However, we expect the Central Bank to continue signalling its commitment to price stability with another hike in the monetary policy rate, but at a slower pace than the previous increase in March 2023.

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