

# FUNDAMENTALS

# NIGERIA'S JUNE 2023

# CPI UPDATE:

# UNEASY CALM

A large orange circle with a diagonal line pattern is positioned in the bottom left. To its right, two smaller orange circles are stacked vertically, with a grey shadow effect behind them.

20 JULY 2023



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## IN BRIEF

- Nigeria's headline inflation continued its upward trend in June 2023, albeit at a slower-than-expected pace, standing at 22.8% y/y in the month under review (-38bps compared to May 2023). The increase was mainly driven by food inflation, which recorded its strongest rise since September 2005, to hit 25.3% y/y in June 2023 (+44bps).
- Notwithstanding the authorities' measures to unify the multiple exchange rate markets, we observed renewed widening of the spread between the parallel market rates and the official rate on the Investors' & Exporters' window. We expect the higher USD/NGN to sustain the elevated fuel prices and utility tariffs with upside risk to the near-term inflation.
- The effects of recent fuel subsidy removal with resultant spike in fuel and transport costs were not fully visible in the June 2023 Consumer Price Index (CPI). We believe this muted impact reflects policy time lag as only approximately two weeks of the policy measures were captured in the consumer price data. This time lag suggests continued upside risk over the coming months, making the slight uptick in the June 2023 inflation rate appear as an uneasy calm.
- The Monetary Policy Committee (MPC) will convene from 24<sup>th</sup> – 25<sup>th</sup> July 2023 for the first MPC meeting following President Bola Tinubu's removal of fuel subsidies and easing of constraints on foreign exchange trading. Given the surprisingly subdued increase in the first post-reforms inflation, we anticipate the monetary policy review to focus on the magnitude of anticipated increase in the policy rate. We believe a marginal increase of 25bps to 18.75% would balance between the need to restore price stability and the risk to a weakening non-oil economic activity.

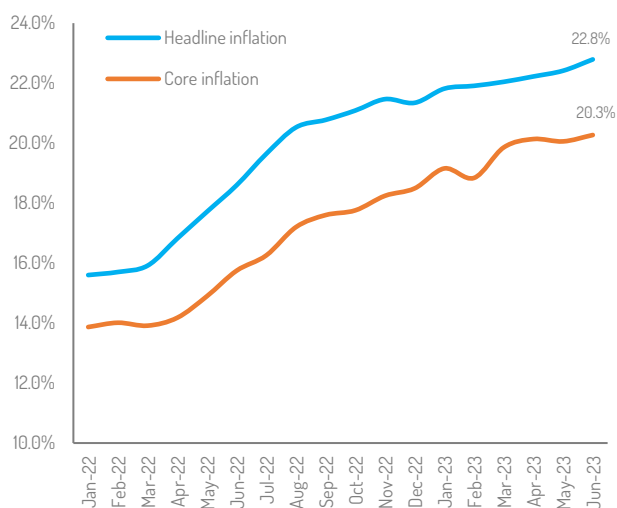
## Nigeria is not out of the woods

Nigeria's headline inflation continued its upward trend in June 2023, albeit at a slower-than-expected pace, standing at 22.8% y/y in the month under review (+38bps compared to May 2023). The increase was mainly driven by food inflation which recorded its strongest rise since September 2005 to hit 25.3% y/y in June 2023 due to higher prices for Oil & fat, Tubers, Bread & cereals, Vegetables, Fish, and Meat.

The increase in headline inflation partly reflects the impact of recent removal of fuel subsidies, higher transport fares, and the unification of Naira exchange rates. Following the removal of fuel subsidies in late May 2023, we observed an immediate spike of 172% in ex-pump prices to -NGN 500 per litre. The higher fuel cost triggered a domino effect on transport fares, and the prices of goods and services.

We also observed price pressures in core inflation (the overall CPI excluding prices of volatile agricultural produce). Consequently, the 8bps decline in core inflation for May 2023 was reversed with a 20bps increase to 20.3% y/y in June 2023.

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



Source: National Bureau of Statistics

Despite the uptick in all measures of CPI inflation, we believe the effects of recent fuel subsidy removal with resultant spike in fuel and transport costs were not fully visible in the June 2023 Consumer Price Index (CPI). In our view, this muted impact reflects policy time lag as only approximately two weeks of the policy measures were captured in the consumer price data. This time lag suggests continued upside risk over the coming months, making the

slight uptick in the June 2023 inflation rate appear as an uneasy calm.

Notwithstanding the authorities' measures to unify the multiple exchange rate markets, we observed renewed widening of the spread between the parallel market rates and the official rate on the Investors' & Exporters' (I&E) window. As of 19 July 2023, the I&E rate closed trading at NGN790.51/USD, representing a 16.3% depreciation since the devaluation in mid-June. However, FX supply on the I&E market has tightened throughout July 2023 with a resultant demand spillover to the parallel market. We expect the higher USD/NGN to sustain the elevated fuel prices and utility tariffs with upside risk to near-term inflation.

In March 2023, the Food & Agriculture Organisation (FAO) projected ~25.3 million people in Nigeria to face acute food insecurity during the June to August 2023 lean season. Last week, the Nigerian authorities declared a state of emergency on food security as price pressures intensify across basic food items. While we expect the provision of fertilizers and cereals to farmers and households to partly mitigate the effect of the removal of fuel subsidies, we foresee continued pressure on food prices in the months ahead. With the lean season in full swing, we expect the tight agrarian supply to sustain the food price pressure amidst the higher transport fares.

### The Monetary Policy Committee will continue on a restrictive policy path

The Monetary Policy Committee will convene on 24<sup>th</sup> – 25<sup>th</sup> July 2023 for the first MPC meeting following President Bola Tinubu's removal of fuel subsidies and easing of constraints on foreign exchange trading. Given the elevated uncertainty to the inflation outlook, we believe the MPC would need to continue signalling commitment to restore price stability. Consequently, we anticipate the monetary policy review to focus on the magnitude of anticipated increase in the policy rate. We, thus, foresee a marginal increase of 25bps to 18.75%, which would balance between the need to restore price stability and the risk to a weakening non-oil economic activity.





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