

HEADLINE INFLATION RISES TO 21.09%

... Month-on-Month Pressures Further Moderates

November 16, 2022

Economic Report

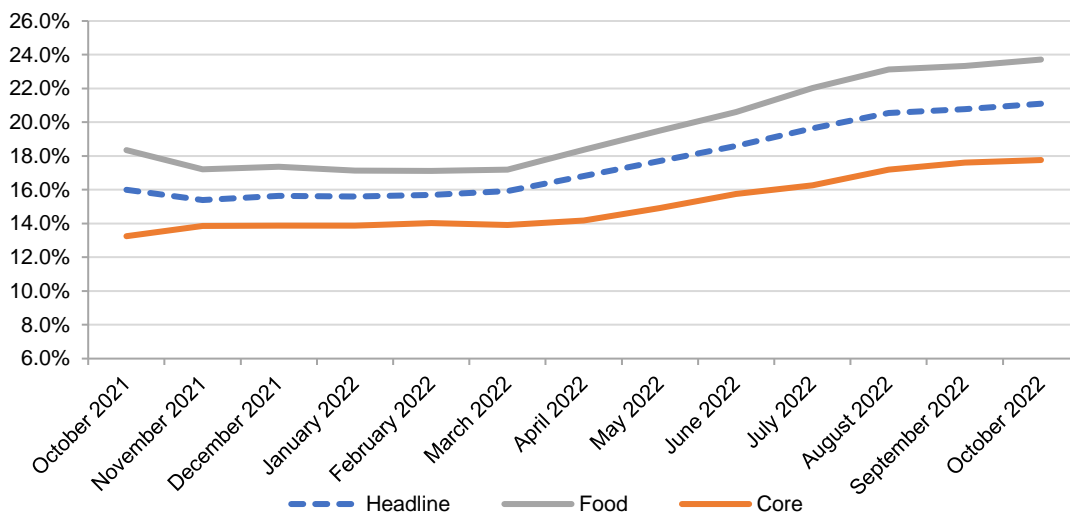
Highlights

Headline Inflation accelerated further in October 2022, with the figure printing 21.09% year-on-year (September 2022: 20.77%) - the ninth consecutive upward trend since February 2022.

The sub-components of inflation, Core Inflation and Food Inflation rose to 17.76% (September 2022: 17.60%) and 23.72% (September 2022: 23.34%) on a year-on-year basis, respectively.

However, on a month-on-month basis, the numbers moderated, as Headline Inflation declined to 1.24% in October 2022 from 1.36% in September 2022. In the same vein, Food Inflation declined to 1.23% in October 2022 from 1.43% in September 2022, while Core Inflation declined in October 2022 to 0.93% from 1.59% in September 2022.

One-Year Inflation Trend



Source: National Bureau of Statistics, WSTC Research

Analysis

We attribute the month-on-month moderation in inflation to a slowdown of price pressures in the global commodities market during the period. According to data from the World Bank, the fertiliser index declined to 214.26 points in October 2022 from 222.51 points in September 2022. We note that the index rose to a 5-year high of 254.97 points in May 2022. Other possible factors that induced lower pressures on food prices were improved security in food-producing regions and increased supply due to the harvest season. On a year-on-year basis, however, inflation rose as prices remained above historical levels even though there was a recent moderation in the pressure.



Energy price pressures also cooled in October 2022, as indicated by the month-on-month Core Inflation decline. We attribute this to a pullback in oil prices due to fears that rising interest rates could induce a global economic recession and result in lower future oil demand. However, the current price levels are still above the recent historical trend.

Outlook

We expect the month-on-month moderation in prices to be short-lived, based on our postulation that the recent flooding in major parts of the country would constrain food supply and other economic activities. We see this risk fully reflected in the near-term inflation numbers. Therefore, we expect much higher inflation readings in the subsequent months.

Expected Policy Response

We do not expect the tightening stance of the monetary policy authorities to change. We note the recent Naira redesign policy aimed at addressing specific issues such as hoarding of bank notes, risk of counterfeiting, and worsening shortage of clean notes. In our view, the bigger picture might be to manage the money supply as part of the efforts to combat inflationary pressures. Since the policy announcement, the exchange rate in the parallel market rose to as high as N850 before retreating to c.N700 levels. While we are still in the early days of the Naira redesign policy, we do not think that the policy initiative would have any material impact in stabilising either the FX market or domestic inflation.

In our view, CRR and fixed-income yields would be more effective. On a broader scale, we note that the underlying drivers of inflation are structural in nature. Hence, while we may see shifts and twists, the high inflation level is likely to remain in the near term.

Implications for the Financial Markets

Fixed Income: yields in the fixed income market are expected to maintain an upward trajectory due to the current policy stance of the monetary policy authorities.

Equities: the NGX All-Share Index is currently down by 15.46% in H2 2022 after an initial 21.31% price appreciation in H1 2022. We expect investor interest in equities to remain weak owing to two main factors. The first is illiquidity - relating to foreign exchange and inconsistent FX policies. The second is higher fixed-income yields which imply higher opportunity costs.

Foreign Exchange: given the recent headline inflation reading, the justification for holding the Naira as a store of value continues to weaken. Therefore, we expect investors to consider foreign assets that are better stores of value. By implication, we see the demand for the USD increasing in the near term. The supply of FX is still weak, in our view. Therefore, we expect the exchange rate to trade higher, particularly in parallel markets.

**Other Highlights**

Indexes	Year-on-Year Change			Month-on-Month Change		
	Oct 2022	Sept 2022	Bps	Oct 2022	Sept 2022	bps
	%	%		%	%	
All-items Price Index	21.09	20.77	32	1.24	1.36	(15)
Food Index	23.72	23.34	39	1.23	1.43	(20)
Core Index	17.76	17.60	16	0.93	1.59	(66)
Urban All-items Index	21.63	21.25	38	1.33	1.46	(13)
Rural All-items Index	20.57	20.32	25	1.16	1.27	(11)

Source: National Bureau of Statistics, WSTC Research



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- Buy Rating: estimated fair value is $\geq 15\%$ above current market price.
- Hold Rating: estimated change in price is between -10% and 15% of current market price.
- Sell Rating: estimated change in price is $\leq -10\%$ of current market price.

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