KPMG

Flashnotes

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- **Nigeria's annual Inflation rate remained high and largely unchanged across all categories in February 2023.**
- **The cash crunch which has affected consumers expenditure following the earlier redesign of the naira, doesn't seem to have slowed down inflation yet, despite a 500-basis interest rate hike since May 2022 and a 235% decline in cash in circulation.**
- **CBN likely to maintain its hawkish stance on rates when the MPC meets 20-21 March, while it waits to assess Q1 2023 GDP results**

Event

The National Bureau of Statistics has published its Consumer Price Index (CPI) report for February 2023. The CPI, a closely watched gauge of inflation, showed that annual price changes remained high and rising in February. The headline CPI for February measured 21.89% (a new two decade high) compared to 21.82% in January. On a monthly basis, however, prices slowed by 1.71% compared to the January monthly rate of 1.81%.

Food prices, which dominates the CPI basket, were the largest contributor to the increase in inflation with food inflation rising to 24.35% compared to 24.32% in January, while monthly, food prices rose slower at 1.90% compared to 2.08%.

When stripping out volatile energy and food prices, core CPI slowed both on an annual and monthly basis by 18.84% (from 19.16% in January) and 1.06%(from 1.82%) respectively.

Analysis/Opinion

Nigeria's inflation is caused by a complex mix of demand pull and cost push factors.

Following the CBN's currency redesign policy, currency in circulation has dropped from N3.28 trillion in December 2022 to N1.38 trillion in January and estimated N982.09 billion in February 2023, representing a 235% decline. It was expected that the scarcity of redesigned notes, which caused a cash crunch in the economy since January 2023, would stimulate a slowdown in demand pull inflation, especially given the series of interest rate hikes from the Central Bank (500 basis points since May 2022). This has however, not happened yet.

Date	Currency in Circulation (Trillions of Naira)
September 2022	3.350
October 2022	3.245
November 2022	3.250
December 2022	3.288
January 2023	1.386
February 2023*	0.980

Source: ***CBN *Estimated***

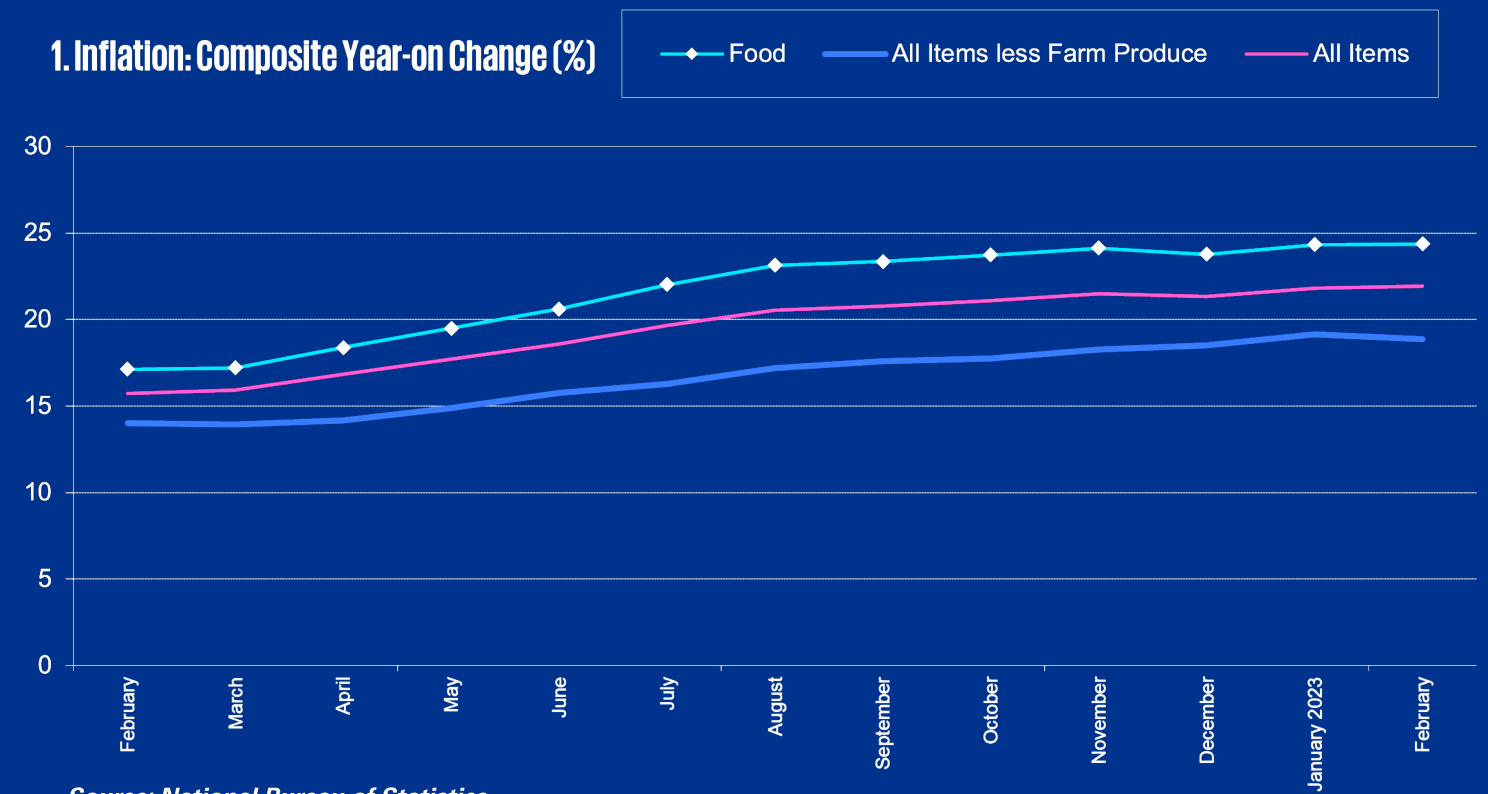
This might indicate a drop in output below effective demand, despite the cash crunch, with some producers of goods and services whose activities are cash based facing challenges purchasing inputs for production or replacing their stock and distributing them across the country.

The continuing rise in inflation rate may also suggest that persisting cost push factors remain clear and present determinants of the direction of inflation. These include structural issues which impact domestic food production and transportation, such as insecurity, floods in key agricultural producing areas, exchange rate challenges and rising international food and energy prices following the Russia-Ukraine crisis. Accordingly, it suggests, policy measures targeted at controlling spending may not be the most preferable strategy for controlling current inflation trends.

Our assumption that many of these factors above will be maintained in 2023 informs our expectation of sustained high double-digit inflation in 2023. We estimate about 30-40% of largely informal sector economic activity before the cash redesign policy was cash based and while we expect some of these would have switched to electronic based transactions, we do not believe enough time has elapsed for it to have been fully and effectively substituted. Additionally, the expected fuel subsidy removal advocated by both the current and the incoming administration, if it does materialize, and the 2022 Fiscal Bill to be introduced in 2023 are also expected to keep pressure on domestic prices in 2023
.
Furthermore, we expect the decision of the CBN to recirculate the old naira notes would delay the full switch to electronic transactions but to have a minimal impact on cash availability constraints, given that CBN has indicated that a large portion of the old notes have already been destroyed.

That being said, we expect the CBN to retain its hawkish stance on interest rates when it meets on the 20th and 21st of March, until it has had a chance to assess the results of Q1 2023 GDP due to be published in May 2023

1. Inflation: Composite Year-on Change (%)



Source: National Bureau of Statistics

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