Sustained disinflation in July as headline inflation prints at 17.38%

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Economics | Data Reaction

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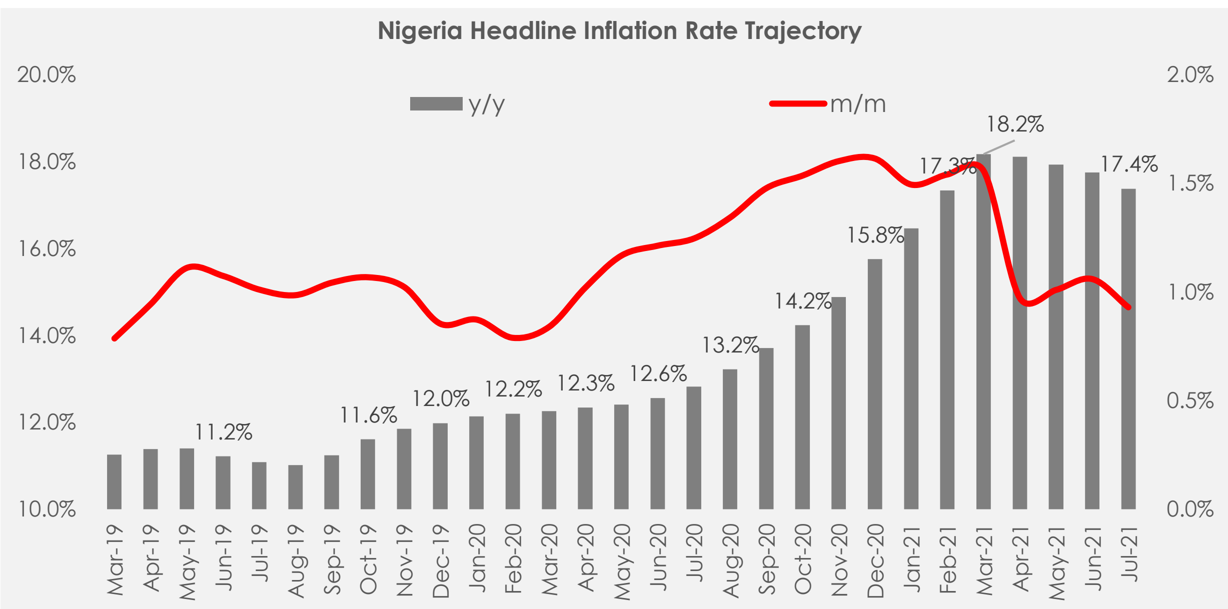
Food sub-index	Core sub-index	Headline Index
21.03%	**13.72%**	**17.38%**

Yesterday, the National Bureau of Statistics (NBS) released the inflation report for Jul-2021. Notably, the headline rate rose by 17.38% y/y, lower than our forecast of 17.58% and consensus forecast of 17.50%. This is 37bps lower than the rate recorded for Jun-2021 (17.75%), implying that prices continued to rise in Jul-2021 but at a markedly slower pace than Jun-2021. On a m/m basis, the headline inflation rate declined to 0.93% m/m (vs. 1.06% in Jun-2021). Also, the inflation report confirmed observation of price increase across all components of the index with the highest increases expectedly recorded in food prices.



Sources: NBS, United Capital Research

On a segmented basis, food inflation printed at 21.03% y/y for Jul-2021 compared to 21.83% in Jun-2021, an 80bps decline. On a m/m basis, the Food sub-index increased by 0.86% in Jul-2021, down 29bps from 1.15% in Jun-2021. The moderation in food prices was driven by a high base for the Food sub-index as food prices remained elevated due to prevailing supply-side challenges.

The core inflation sub-index drifted northwards to 13.72%, a 63bps increase from June 2021's 13.09%, reflecting renewed pressure on textile products, transportation & vehicle spare parts and pharmaceutical products. Similarly, on a m/m basis, core inflation increased by 50bps in

Jul-2021 to 1.31% compared to 0.81% in Jun-2021. Clearly, core inflation continues to face lingering pressures from healthcare costs (impacted by the pandemic and recent surge in Covid-19 cases) and imported consumption of household appliances (due to naira devaluation).

Inflation Outlook: Disinflation to persist despite underlying pressures

Looking ahead, we note that price pressures still abound in the economy. Insecurity remains a significant and worrisome constraint on food supply as banditry remained rampant during the period under review. Furthermore, the decision taken by the CBN to halt the sale of foreign exchange to Bureau De Change (BDC) operators in late Jul-2021 is likely to trigger inflationary pressures albeit minimal, going by the sustained pressure on the parallel market rate. Nonetheless, we expect the headline rate to moderate further in Aug-2021. This expectation of further disinflation remains hinged on the high base effect from H2-2020. However, while we observe that the pace of disinflation has quickened in recent months (from 5bps in Apr-2021 to 37bps in Jul-2021), we expect a reduced pace in Aug-2021 due to likely FX-linked pressures. For Aug-2021, we forecast annual headline inflation to drift lower by 28bps to 17.10%.

The longer-term prognosis for H2-2021 favours disinflation as well, albeit it is more muted. We expect the FG to move ahead with cutting subsidy payments, at least partially, which will invariably feed inflationary pressures. Despite the bleak horizon, we expect the effects to be overshadowed by the high base impact highlighted earlier. Our optimism is also hinged on a critical driver of inflation, foreign exchange. We expect to see renewed stability in the FX market as oil prices are expected to remain strong coupled with improved production, while the impending Eurobond issuance and the Special Drawing Rights (SDR) allocation from the International Monetary Fund (IMF) would support external reserves accretion. Thus, FX-linked pressure on inflation in H2-2021 will be reduced, supporting further disinflation.

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