CAPE
Economic Research & Consulting

Cape Economic Performance and Prospect Bulletin – February 2023

Highlights

- *Price pressures expected to remain heightened above pandemic levels as tightening efforts continue to crystalise.*
- *Nigeria's Q1 2024 output growth expected to remain positive and higher than the 2.11 per cent anticipated in Q4 2023.*
- ***Forecast shows that inflationary pressure in Nigeria heightened in January 2024, with headline inflation rising to 29.69 per cent**.*

Global Economic Update

The global economy continues to exhibit notable resilience, as prices maintain broad moderation and growth subsist. The prospects of a "soft landing" continues to heighten, although the expansion pace has not yet caught up. On the demand side, global activity has been supported by robust public and private consumption, despite tight monetary conditions. On the supply side, increased participation of labour force, restored supply chains, and lower factor costs energy and commodity prices helped, amidst worsening geopolitical uncertainties.

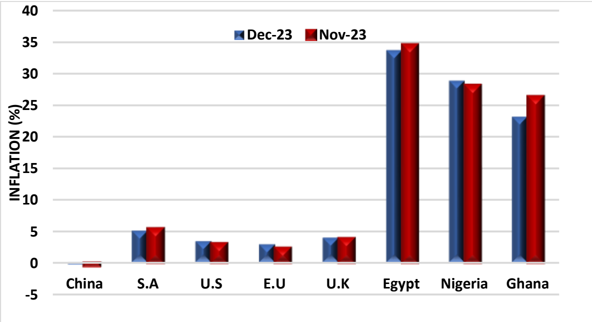
Divergent growth prospects across regions remains a challenge to global full recovery to pre-pandemic levels. In the advanced economies, despite the tight monetary policy stance, several economies showed significant resilience and circumvented a hitherto anticipated recession, albeit with an abysmal growth performance. In emerging economies, concerns about China's capacity to boost its economy dampened growth prospects despite the significant level of resilience posed by several individual countries.

Overall, major headwinds to output growth are weak consumer demand, geopolitical fragmentation, full impact of tight monetary and financial conditions.

In terms of inflation, a lot of advanced and emerging economies have turned the curve, although pressure on households remains acute and the cost of living remains high. Inflation upside risks include the Israel-Hamas conflict and Russia's war in Ukraine which continued to affect prices for commodities, such as oil and grains.

Gains in the widespread policy rate hikes across both advanced and emerging economies to rein-in inflation remain divergent across economies. Specifically, headline inflation continues to moderate across several economies, although, core inflation moderated slightly, it remains largely stickier than anticipated. The pressure on many households remains acute, and the cost of living remains high, though at a reduced level of intensity particularly in some advanced economies.

Figure 1: Year-on-Year Inflation in Selected Economies (November 2023 – December 2023) in per cent



Source: Various National Statistics Offices

Policy rates in advanced economies have either reached their peak or are about to in this cycle as central banks see increasing evidence that tighter financing conditions are starting to bite.

We anticipate that several central banks will maintain a hold or tightening stance at least for the first half of 2024, although at a moderate pace to effectively dampen price pressures, bearing in mind trade-off implications for the fragile output growth and financial system stability. We anticipate a gradual return to a loose stance as the year goes by into 2025. The return to loosening is precipitated on the risk of further rate hikes dampening inflationary pressure but heightening financial system instability and dragging economies into recession.

In the financial markets, stock and bond market performance moderated and diverged in January from the broad-based year-end rally. Long yields in the US, UK and Europe rose from their year-end lows challenging long-duration bond performance, as markets recalibrated expectations for the timing of anticipated policy rate cuts. The focus on politics will also continue to grow, as the possible Biden-Trump rematch buzz has already started to filter into the general public, even though the primaries have just started. Typically, the Street will start to take market positions on the expected November outcome in September, as a clearer picture on not just the presidency emerges, but that of the House and Senate.

In the currency market, US dollar ended the first month of the new year with a stellar performance, leading all major rivals by a considerable margin, while yen ended the month at the tail end of the list, marking the worst performance since February 2023. The powerful start by the US dollar came amid the bullish stance by the Federal Reserve, which hurt the odds of an early interest rate cut in March 2024. Additionally, a string of recent strong US data and bullish remarks by Fed officials underpinned the dollar further.

In the commodities market, the price of gold declined by 2.1% in January to US$2,018.50 per ounce, as the precious metal market continue to be influenced by the stance of monetary policy. Crude oil prices pushed higher in January; the price of WTI ended the month at US$75.84 per barrel while Brent was US$83.99, with respective monthly increases of 6.9% and 8.1%. As winter persists and energy demand surges, it is anticipated that oil prices may remain high.

Upside risks to energy and commodity prices remain increased demand, while the pressure in the financial system and the risk of a recession are downside risks. The rising geopolitical tension, including the war in Gaza and the war between Russia and Ukraine continue to disrupt supply and cause shortages of major staples such as wheat amongst others and exerts significant pressure on food prices across countries.

Global Economic Outlook

The global economy continued to show resilience in the first quarter of 2024, despite several headwinds and geopolitical fragmentation. Downside risks remain – as the core inflation remains stubborn and central banks are second guessing commencing a loosening stance as early as possible in 2024. Others include, heightening geopolitical tensions, tight financial conditions, and weak export demand.

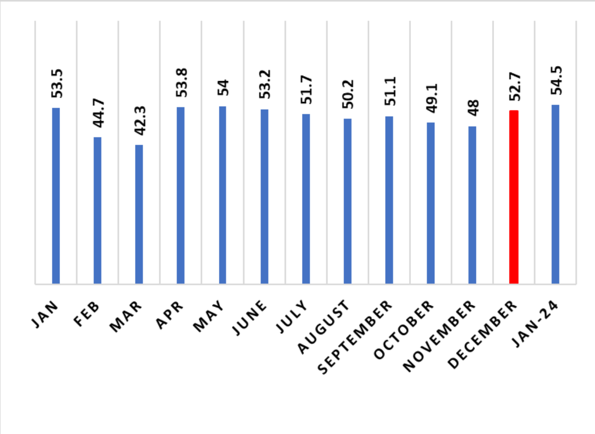
Consequently, we expect slower growth in the United States, where tight monetary policy is still working through the economy. And in China, where weaker consumption and investment continue to weigh on activity. In the Euro area, activity is expected to rebound marginally. In Sub-Saharan Africa, despite weakening regional blocs, growth is expected to rise, as the negative effects of earlier weather shocks subside, and supply issues gradually improve.

In the financial markets, we anticipate that as policy rates begin to slow down, there might be some gradual portfolio flow gains to emerging markets, where rates are likely to remain higher in the near to medium term, while others may seek haven in commodity assets and bonds as yields are near 20-year high across sectors. Central banks continue to be faced with a more difficult decision reaching process as the cost to financial stability and output growth are becoming more visible in the first quarter of 2024. On the one hand a premature easing of financial condition would revert the gains in taming inflation, on the other hand however, further tightening could worsen financial instability and tilt the economy into a recession. Major upside risks to inflation remain supply disruptions due to the war in Gaza and Ukraine lingering effects of the pandemic and change in climatic conditions.

Nigeria’s Output Growth

Amid elevated inflation, deteriorating exchange rate, rising insecurity and other macroeconomic impediments, private sector business activity in January 2024 sustained the momentum of its recovery. This comes on the heel of the significant expansion of Stanbic-IBTC headline purchasing managers’ index (PMI), which rose to 54.5 in January 2024 from the December 2023 print of 52.7 index points. In January, business activity recorded growth for the second month in a row, reaching its highest rate in 21 months. The increase in January PMI was driven mainly by substantial growth in new orders and output, indicating sustained robust demand.

Figure 2: Trend of Nigeria's PMI (Jan 2023– Jan. 2024)



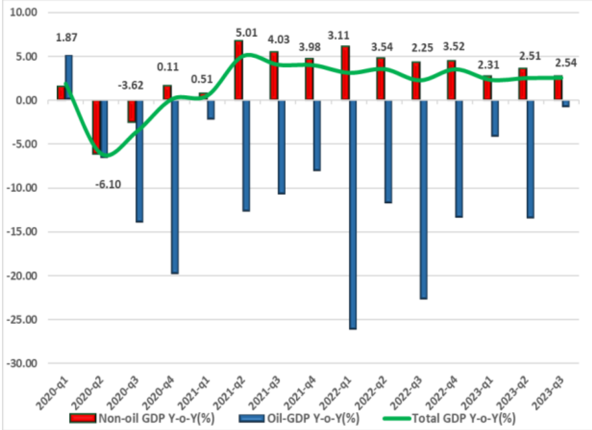
Source: Stanbic IBTC

During the period under review, stock accumulation by companies signalled plans for further improvements of output in the months ahead, thus expressing optimism that output would continue to expand. Consequently, employment increased at a milder rate in January 2024. As a guide, a PMI reading surpassing 50.0 signifies an enhancement in business conditions, whereas readings below 50.0 suggest a deterioration in business conditions compared to the previous month. A PMI reading of 50.0 denotes a situation where there is no change in output growth.

Nigeria's real GDP growth in the first quarter of 2024 is therefore expected to improve slightly owing to the resilience of economy inspite of the multiple headwinds.

Reflecting on 2023, the expected annual real GDP growth for Nigeria is projected to be approximately 2.5 percent (figure 3) owing to the harsh macroeconomic conditions throughout the year. This growth rate notably falls below what would be considered adequate for improving the welfare of citizens, especially in an economy marked by an annual population growth of around 3.0 percent. Sustained policy reforms are required to change the growth narrative of Nigeria in 2024.

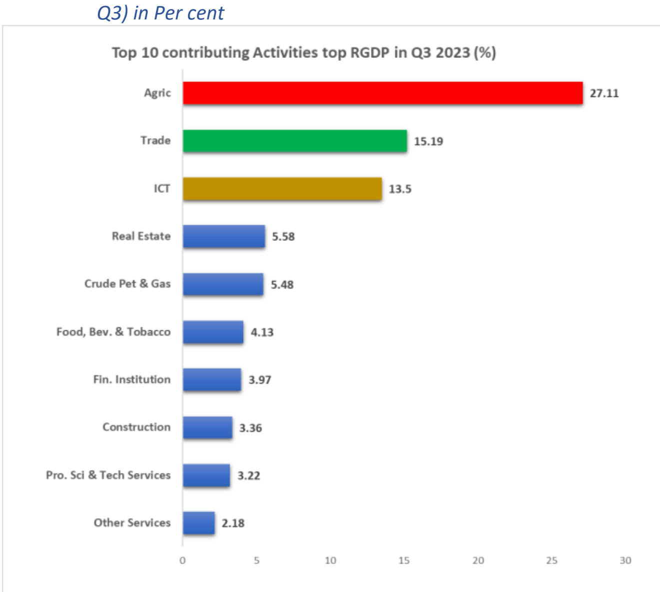
Figure 3: Real GDP Growth Rate in Nigeria (2020Q1 – 2023 Q3) in Per cent



Source: National Bureau of Statistics (NBS)

The primary economic drivers of real GDP in 2023, notably during Q3, comprise of sectors such as agriculture, trade, information and communication (ICT), real estate, and various others (figure 4).

Figure 4: Top 10 Economic activities that drove Nigeria's RGDP (2023 Q3) in Per cent



Source: National Bureau of Statistics (NBS)

Output Growth Outlook

Output growth continues to be resilient despite several headwinds confronting it. High energy prices, exchange rate volatility arising from foreign exchange supply shortage, insecurity, infrastructural deficit, structural bottlenecks, and elevated cost of production continue to weigh on output growth. Consequently, it is expected that output growth would further slowdown albeit remain positive in 2023Q4. Moreover, several multinationals have abandoned domestic production in 2023Q3 and 2023Q4 due to rising cost of production and difficulty in profit repatriation with implications for output growth and employment. Our medium-term forecast show that output growth would moderate to 2.11 per cent in 2023Q4. We however anticipate an improvement in output growth going into 2024Q1, as seasonal benefits in the agricultural sector kicks and the gains from improvement in the industrial sector with the coming on stream of companies such as the Dangote refinery by 2024Q2.

Table 1: Medium-term Macroeconomic Forecast in Per Cent

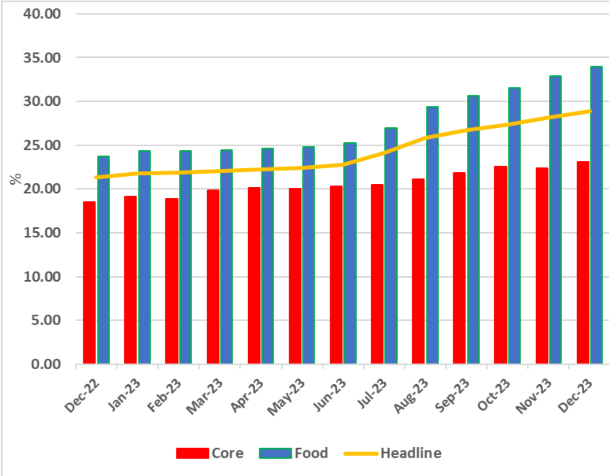
	2022q3	2022q4	2023q1	2023q2	2023q3	2023q4	2024q1	2024q2	2024q3
Output (year % change)									
Real GDP	2.25	3.52	2.31	2.51	2.54	2.11	2.74	2.72	2.34
Manufacturing	-1.9	2.8	1.6	2.2	1.5	0	-0.1	4	2.4
Agriculture	1.34	2.05	-0.9	1.5	1.53	0.13	3.69	0.33	0.68
Trade	5.08	4.54	1.31	2.41	2.08	0.62	3.37	2.42	2.53
Information & Comm.	10.1	11.2	11.7	9.7	9.9	6	14.2	7.4	8.8
Inflation (yr % ch.)									
Headline	20.3	21.3	21.9	22.5	25.5	27.5	27.8	27.6	27
Food	22.8	23.9	24.4	24.9	29	31.6	31.9	31.4	28.9
Core	17	18.2	19.3	20.2	21.5	22.9	22.6	22.2	21.2

Source: CAPE Economic Research and Consulting, 2023

Price Update

Nigeria's headline inflation soared higher in December 2023, reaching 28.92 per cent relative to the 28.2 per cent recorded in November 2023. Similarly, food inflation surged to 33.93 per cent from the 32.82 per cent reported in the previous month. In the same vein, core inflation rose to 23.06 per cent compared to the 22.38 per cent printed in November 2023. The upward trajectory was driven mainly by worsening foreign exchange situation, higher energy prices, build-up of aggregate demand during the yuletide season and other structural bottlenecks that characterises the Nigerian economy.

Figure 5: Year-on-Year Headline, Food and Core Inflation (Dec 2022 – Dec 2023) in per cent



Source: National Bureau of Statistics (NBS), 2023

Price Outlook

Inflation is expected to further heighten in January 2024. Our forecast showed that inflationary pressure would be elevated as headline and food inflation are expected to rise to 29.69 and 35.21 per cent respectively, while core inflation is expected to moderate marginally to 22.63 per cent respectively.

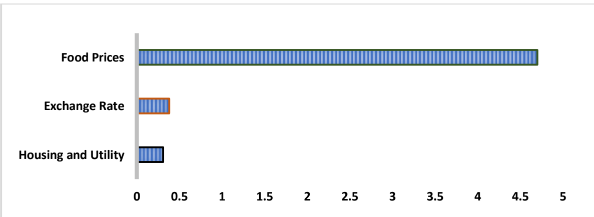
Table 2: Inflation forecast for January 2023 in Per Cent

Headline	Food	Core
29.69	35.21	22.63

Source: CAPE Economic Research and Consulting, 2023

The key drivers of the headline inflation forecast remained, food prices, exchange rate, housing and utility prices which contribute 4.70 per cent, 0.38 per cent, and 0.31 per cent respectively.

Figure 6: Driver of Predicted Inflation

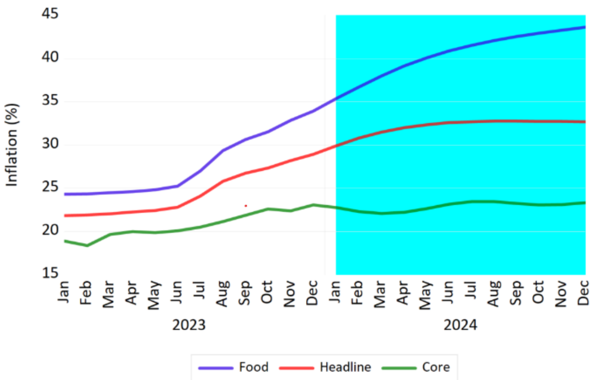


Source: CAPE Economic Research and Consulting, 2023

Our analysis showed a strong impact of food prices, exchange rate, housing and utility on headline inflation. This suggests that the impact of increase in energy prices and exchange rate as a result of deregulation in June 2023 continues to permeate into the economy and would continue to reflect over a 12-month period at the least, through a base effect.

The key drivers of core inflation forecast were transportation, education, clothing, housing and utility and health. Upside risks to inflation remain high fiscal deficit, removal of fuel subsidy and exacerbating exchange rate pressures as well as its pass through to prices. Economic agents remain expectant of actions and policy direction of the new leadership at the Central Bank of Nigeria as it did not hold any Monetary Policy Committee (MPC) meeting in 2023Q4. It is expected that first MPC meeting of the newly appointed Committee of Governors would hold in February 2024. Going by the dearth of monetary policy actions since its last meeting in July 2023, it is expected that the MPC at its February 2024 meeting would hike by at least 200 basis point considering the wide margin of negative real rates. Moreover, it is our view that the monetary conditions in the Nigerian economy, remain relatively loose, which is also heightening the pressure in the foreign exchange market. While we are aware of the need for improved coordination between fiscal and monetary policy in Nigeria in a bid to halt its fast deteriorating economic conditions, it is our view that the MPC would need to resort to an aggressive quantitative tightening to play its own part of the much needed policy responses.

Figure 7: 12-Month Inflation Projection



Source: CAPE Economic Research and Consulting, 2023

Our revised 12-month inflation projection suggest that inflation would remain elevated, but the pace of elevation would remain moderated as headline inflation plateaus in the second half of 2024.

Fiscal Operations Update

The Federation Account Allocation Committee (FAAC) distributed the total sum of N1,127.41 billion among the three tiers of government in the month of January 2024 for revenue collected in December 2023. The amount distributed was higher than the N1,088.79 billion shared in December 2023 by N38.62 billion representing an increase of 3.5 per cent. The increase was driven mainly by non-oil revenue, specifically, value-added tax (VAT), corporate tax (CIT) and customs & excise duties.

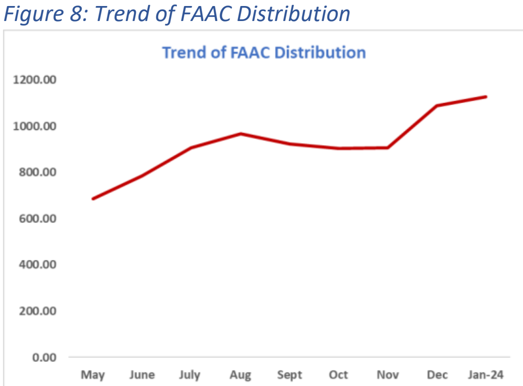
Table 3: Highlight of Jan 2024 FAAC Distribution (N'billion)

	Jan 2024	Dec	% Change
Fed.	*383.87*	*402.87*	-4.7
State	*396.69*	*351.70*	12.8
LG	*288.93*	*258.81*	11.6
13%	*57.92*	*74.41*	-22.2
Total	**1,127.41**	**1088.79**	3.5

Source: FAAC, January 2024

Further breakdown shows that Federal Government received N383.87 billion; States, N396.69 billion; Local Government, N288.93 billion. Thirteen per cent derivation fund distributed among beneficiary states amounted to N57.92 billion. While revenue allocation to States and Local Governments increased by 12.8 and 11.6 per cents, allocation to the Federal Government declined by 4.7 per cent. Increase in FAAC allocation would allow subnational government implement the 2024 budget. However, it also represents a boost to liquidity which may contribute to inflationary build-up in January 2023.

Figure 8: Trend of FAAC Distribution



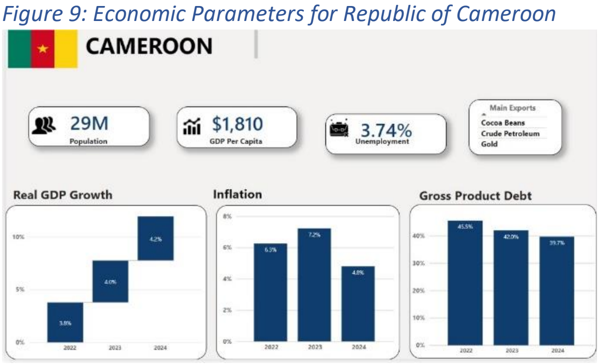
Source: FAAC, January 2024

Conclusion

In conclusion, prospect for global output growth for 2024 remains positive but weak. Prospects in emerging economies is signifcantly challenged by uncertainty and weak performance of China. The tight stance of most central banks across both advanced and emerging markets for the most of 2022 and 2023 has started yielding results in price moderations in some economies. However, this comes with a significant moderation to output and financial stability. In Nigeria, economic prospects for the fourth quarter of 2023 and going into 2024 remains resilient, albeit at a moderated level. Moreover, adverse impacts of some of the bold policy reforms embarked on by the government may subsist in the near to medium term, but over the long run, it is anticipated that some respite would follow.

Country in Focus – Republic of Cameroon

Figure 9: Economic Parameters for Republic of Cameroon



Source: CAPE Economic Research and Consulting, 2023