Cape Economic Performance and Prospect Bulletin – July 2024

Highlights

- *Price pressures expected to remain heightened and remain above pandemic levels as tightening efforts continue to crystalise.*
- *Nigeria's Q2 2024 output growth expected to be lower than Q1 2024 but remain positive.*
- ***Forecast shows that inflationary pressure in Nigeria heightened marginally in June 2024, with headline inflation rising to 34.17 percent**.*

Global Economic Update

The global economy continues to show signs of recovery as inflationary pressures continue to dampen, supply bottlenecks ease and job market expand. Global output growth for 2024 is forecast at 2.9 percent, marginally down from 3.1 percent in 2023, amidst persisting political uncertainties persist and permeating impact of elevated interest rates.

In the advanced economies, the US economy continues to outperform expectation, driven by domestic demand spurred by fiscal operations. However, headwinds remain high interest rates, continuing inflation, and high levels of consumer debt, which may eventually dampen consumer spending and overall economic growth. For the eurozone, the forecast for 2024 indicates a positive but modest output growth, despite headwinds from tight monetary policy stance.

Emerging Markets are expected to outpace the growth of advanced economies. China's economic expansion is expected to continue positively in 2024, with a boost from increased investment, despite headwinds from the persisting underperformance of the real estate and weak household spending. Other emerging economies including India, Indonesia, Vietnam, and the Philippines are on pathway to be among the fastest growing economies buoyed by strong domestic consumption and foreign investments. Contrarily, key Latin American emerging markets, including Mexico and Brazil, may be inhibited due to slower demand both domestically and internationally, fiscal consolidation, and strict monetary policies attendant to inflationary pressures.

Overall, major headwinds to output growth remain increasing geopolitical divisions, and the permeating impact of restrictive monetary and fiscal policies.

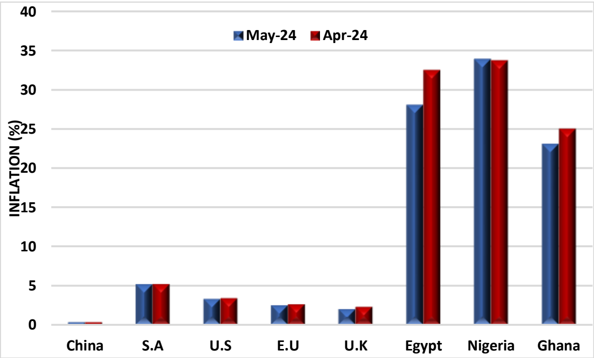
The economic landscape in June was equally shaped by various political developments. The initial presidential debate in the United States concluded with a disconcerting display by Biden, with rising concerns about Bidens candidacy. The ruling parties successfully maintained their positions in India, Mexico, and South Africa. The European Parliamentary elections witnessed a conservative pivot, as the centre-right European People's Party, along with far-right factions, secured additional seats to the detriment of the socialist and environmentalist blocs. Notably, President Macron of France precipitated a snap parliamentary election, resulting in a significant one-third vote share for Le Pen's National Rally in the preliminary round, surpassing Macron's coalition which garnered slightly above 20 percent. Concurrently, the United Kingdom held its general election and the new Prime Minister has formed his cabinet.

Inflationary patterns remain diverse globally, with financial strain on households persisting across economies despite the widespread implementation of hawkish monetary policy stance. The inflationary pressure is further amplified by geopolitical unrest, particularly the Israel-Hamas conflict and the unending military engagement between Russia and Ukraine, which have a pronounced effect on the prices of commodities such as oil and grains as well as climate change concerns in the global logistics which may undermine supply chain. The effectiveness of policy rate hikes aimed at tempering inflation exhibits variability between developed and emerging markets. It is particularly concerning that the diminishing trend of inflation in some advanced economies such as the United States has reversed, and inflation continues to escalate in several emerging economies, mitigating some of the hitherto anticipated positive outcomes.

Efforts to bring inflation down to the target rate of 2 percent have been quite challenging in several advanced economies as inflation has become more sticker as countries move towards the end game in the fight against inflation making easing decision neither easy nor straight forward for central banks to avoid a gains reversal or a premature change in policy stance. A few economies like the UK have achieved the 2 percent target, however it remains cautious.

In the emerging economies, inflation is still largely high, although abating in several economies, but remains above tolerable regions by economies, hence the fight against inflation would continue in those economies.

Figure 1: Year-on-Year Inflation in Selected Economies (April 2024 – May 2024) in percent



Source: Various National Statistics Offices

Policy rates in advanced economies (AEs) seem to have reached their peak for this cycle, as central banks acknowledge the growing impact of tighter financing conditions.

Thus, some AE central banks began their easing cycles in June. Among those, the European Central Bank predictably cut its deposit rate by 25bps, to 3.75 percent, while the Swiss National Bank lowered its policy rate for the second consecutive meeting. Meanwhile, other central banks in AEs such as the US Federal Reserve and Bank of England are taking a cautious approach, opting to wait. The Bank of England although achieved its 2 percent target remains concerned that inflation is stalling at the services level, suggesting it may align with the Federal Reserve's approach regarding the timing and degree of any potential easing. Additionally, in the emerging market, there is considerable pressure for policy easing in China.

We anticipate that several central banks will maintain their tight stance at least for the remainder of the most of the third quarter of 2024, bearing in mind trade-off implications for the fragile output growth and financial system stability. We anticipate a gradual return to a loose stance towards the end of the third and fourth quarter of this year and going into 2025. The return to loosening is precipitated on the risk of further rate hikes dampening inflationary pressure but heightening financial system instability and heightening economic output woes.

In June 2024, equities market reached new peaks, predominantly propelled by the robust performance of the United States market, particularly its AI-related large-capitalization entities. Excluding the US, global equities remained stagnant. Notably, the East Asian emerging markets, especially the semiconductor-heavy economies of Taiwan and South Korea, demonstrated superior performance. The S&P 500® was up 3.47 percent in June, bringing its Year-to-date return to 14.48 percent. The Dow Jones Industrial Average® increased 1.12 percent for the month and was up 3.79 percent Year-to-date. The S&P MidCap 400® lost 1.77 percent for the month, bringing its Year-to-date return to 5.34 percent. The S&P SmallCap 600® was down 2.46 percent in June and down 1.61 percent Year-to-date.

In terms of sovereign debt, ten-year bond yields in the US and Europe experienced a slight decline. An exception to this trend was France, where the yield differential of the French OAT over German bonds expanded following President Macron's unexpected snap elections, although this differential was still narrower than what was observed during the eurozone's debt crisis.

In the currency market, the euro experienced a depreciation relative to the majority of principal currencies. The euro was down 1.3 percent against the dollar in June and was on track for its biggest monthly fall since January as political uncertainty weighed in the run-up to France's general elections. However, it was the Japanese yen that was particularly noteworthy, as it depreciated to its lowest level in several decades against the US dollar and reached an all-time low against the euro. The expectation of policy loosening by the Federal Reserve is likely to decelerate the ascent of the U.S. dollar compared to other principal currencies. However, the robust performance of the U.S. economy and the significant yield disparity in the bond markets are anticipated to forestall any drastic depreciation.

In the commodities market, gold prices remained largely stable and stood around US$2,327 per ounce. The expected rate cuts by the Federal Reserve, may catalyze a sizeable upsurge in gold valuations, although it is assumed that the rate cuts are already priced in. Following a period of stabilization of these increments throughout the summer, it is projected that gold will persist in its upward trajectory amid a backdrop of more accommodative global financial policies. Meanwhile, the crude oil market in June 2024 experienced volatility and an upward price adjustment due to various economic and geopolitical factors. Consequently, crude oil prices experienced a rebound, with WTI ending at US$ per barre81.54 and Brent at US$85.00. Upside risks to energy and commodity prices remain increased demand and geopolitical tensions, while the pressure in the financial system and the risk of a recession are downside risks.

Global Economic Outlook

The global economy has sustained resilience in Q1 2024, despite facing numerous challenges and geopolitical tensions. However, downside risks persist, including the escalating geopolitical tensions, and weak export demand.

In the US output growth will remain positive but lacklustre this year although, as the shift in monetary policy begins to boost spending, growth is expected to pick up next year. Slower wage growth and improved productivity growth will dampen core inflation, triggering a potential rate cut by September this year. However, the forthcoming election induced uncertainty remains of concern. In Europe, modest economic recovery is expected after a prolonged stagnation and as inflation continues to slow down, the ECB would revert to a low interest rate period by Q4 2024 to Q1 2025. Similarly, in the United Kingdom, output growth is expected to expand, and inflation is expected to rate cuts as well are expected. However, outcomes of the July 2024, general election are expected to constituent inconsequential headwind to projections.

In emerging markets, China's economic activity will receive a short-term boost from increased policy support and strong export growth, particularly in industries with overcapacity. However, efforts to support the property sector are proving ineffective. As the benefits from exports diminish and the construction sector faces a downturn, overall growth is expected to slow.

In the financial markets, a further shift of portfolio flows into emerging markets is expected as policy rates are anticipated to commence easing in the advanced economies. Central banks face difficult decisions as the effects on financial stability and economic growth become more pronounced in Q3 2024. Easing financial conditions too early might reverse progress in controlling inflation, while further tightening could lead to financial instability and potentially trigger a recession.

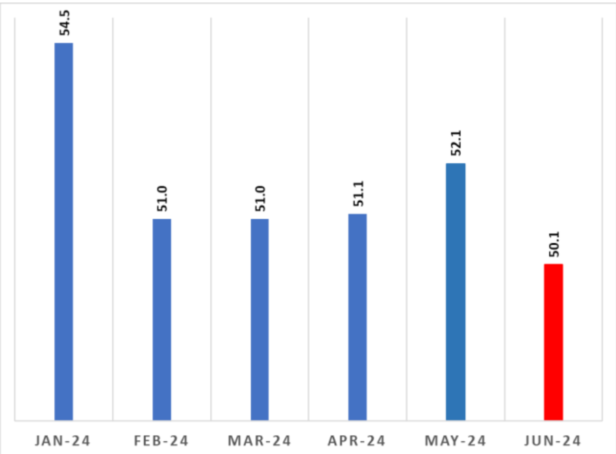
In the commodity market, oil prices are expected to be encumbered in the latter half of 2024 as OPEC+ scales back production cuts. Natural gas and coal prices are projected to drop due to ample supply and high inventory levels. Industrial metal prices are likely to rise driven by China’s easing of fiscal and monetary policies. Gold prices may fall as the positive effects of interest rate cuts are already priced in. Agricultural prices are anticipated to decrease throughout the year owing to an improved supply outlook.

The global economy is contending with a complex mix of geopolitical risks, monetary policy challenges, and commodity market fluctuations. Central banks and policymakers face the difficult task of balancing these factors to maintain growth and stability. This requires careful and strategic interventions to navigate the fragile economic recovery and sustain overall economic stability.

Nigeria’s Output Growth

Nigeria’s growth performance in Q22024 is expected to remain weak, but positive amid aggravating price pressures, rising interest rates, exchange rate depreciation, insecurity and elevated input costs. The Stanbic IBTC headline PMI for June 2024 stood at 50.1 points, slipping to a seven-month low from the 52.1 points recorded in May 2024. PMI readings above 50.0 signals an improvement in business conditions, while readings below 50.0 indicates a worsening business condition compared to the previous month. A PMI of 50 points represents a no-change benchmark. The latest PMI data clearly indicates a decline in private sector economic activities in June 2024. Despite the continued rise in new orders in June, the expansion rate was only marginal and represented the weakest growth observed in the current seven-month period.

Figure 2: Trend of Nigeria’s PMI (Jan - May 2024)

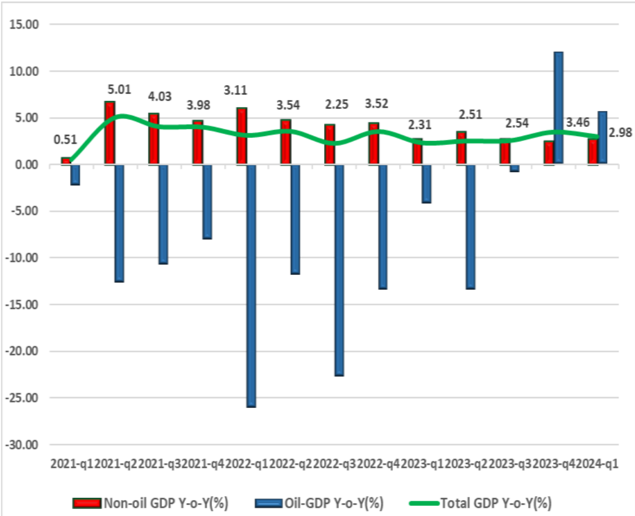


Source: Stanbic IBTC

The sharp plunge in June's PMI to 50.1 point revealed a widespread inactivity within Nigeria's private sector occasioned by a spectrum of macroeconomic headwinds. Subdued demand and heightened price pressures contributed to decelerated growth in both output and new orders. We forecast that domestic demand will remain subdued relative to historical averages, exacerbated by escalating inflationary pressures. Furthermore, the record-high policy rate hikes are expected to persist in exerting a negative impact on the non-oil sectors of the economy.

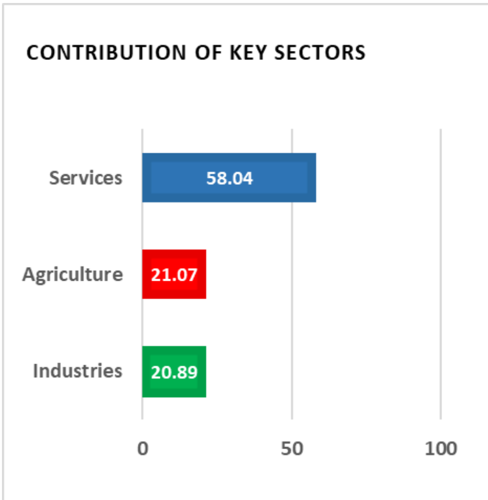
Moreso, looking at the average PMI on quarterly basis, Q22024 PMI stood at 51.1 points, which was lower than the 52.1 points reported in Q12024, suggesting that output growth may be weaker in Q22024, though positive.

Figure 3: Real GDP Growth Rate in Nigeria (Q12021 – Q12024) in Per cent



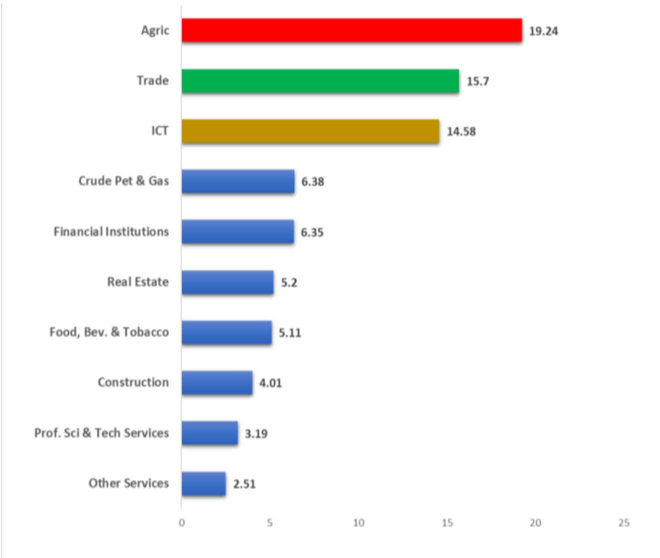
Source: National Bureau of Statistics (NBS)

Figure 4: Sectoral Contribution to GDP in Q12024



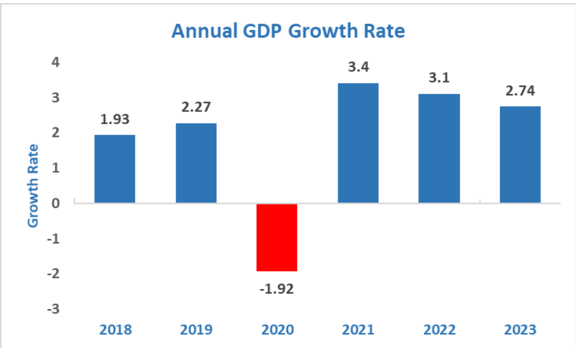
Source: National Bureau of Statistics (NBS)

Figure 5: Top 10 Economic activities that drove Nigeria's RGDP (Q12024) in Per cent



Source: National Bureau of Statistics (NBS)

Figure 6 Year Annual Real GDP Growth (%)



Source: NBS

Output Growth Outlook

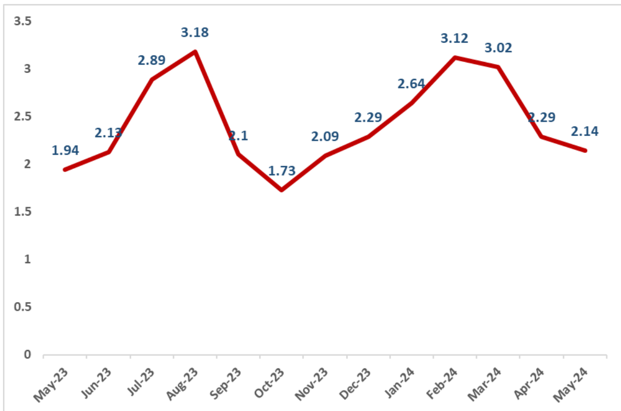
Despite facing numerous challenges, output growth in Nigeria demonstrates resilience. Persistent factors such as elevated energy costs, exchange rate volatility stemming from foreign exchange deficits, security concerns, infrastructural deficiencies, structural barriers, and heightened production expenses continue to hamper growth. As a result, a further deceleration in output growth is expected, albeit remaining positive throughout Q2 and Q3 of 2024.

However, the anticipated upturn in output growth during Q2 2024 is likely to be tempered by various factors, including the monetary policy rate hikes, exchange rate volatility, and mounting uncertainty. Nevertheless, the projected improvement in output can be attributed to seasonal advantages in the agricultural sector and advancements in the industrial sphere, particularly with the commencement of operations at the Dangote refinery anticipated between Q2 and Q3 2024.

Price Update

Inflationary pressure in Nigeria remained elevated as headlined inflation hit 33.95 percent in May 2024 from the 33.69 percent printed in April 2024. This indicated that cost of living in Nigeria rose by 0.26 percentage point in May 2024 compared to the previous month. On a Year-on-year basis, headline inflation rate accelerated by 11.54 percentage points above the 22.41 percent recorded in May 2023, attributed to multiple headwinds including currency devaluation, high energy cost, insecurity among others. However, month-on-month headline inflation rate slowed down for the third consecutive month to 2.14 percent compared to 2.29 percent and 3.02 percent in April and March 2024, respectively *(figure 3***)** This means that rate of increase in the average price level in May 2024 was less than the rate of increase in the average price level in April 2024. ***Thus, the tempo of headline inflation rate is cooling down on a month-on-month basis.***

Figure 8: Headline Inflation month-on-month (May 2023 – May 2024) in per cent



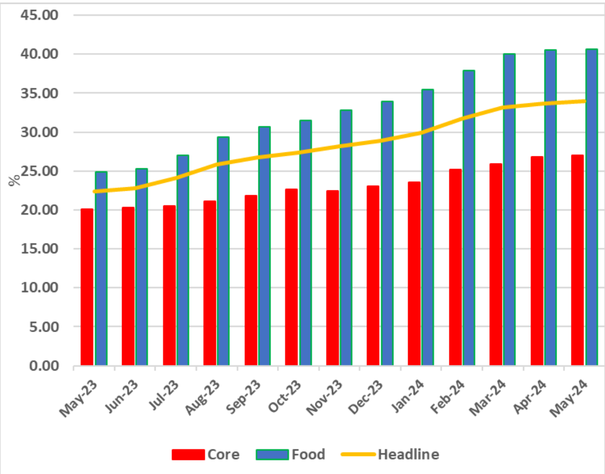
Source: National Bureau of Statistics (NBS), 2024

Food inflation rate in May surged to 40.66 percent from the 40.53 percent recorded in April 2024. On a year-on-year basis, food inflation rose by 15.84 percentage points above the 24.82 percent reported in the corresponding month (May 2023). This was driven by the price increases in essential food items such as Semovita, Oat flake, Yam flour pre-package, Garri, Bean, Irish Potatoes, Yam, Water Yam, Palm Oil, Vegetable Oil, Stockfish, Mudfish, Crayfish, among others. ***However, food inflation also decelerated on a month-on-month basis to 2.28 percent compared to 2.50 percent in April 2024.***

Core inflation rate stood at 27.04 percent, having rose by 7.21 percentage points year-on-year above the 19.83 percent recorded in May 2023. Increase in core inflation was primarily fuelled by rises in the prices of prices of Rents (Actual and Imputed Rentals for Housing Class), Bus Journey intercity, Taxi Journey per drop, etc (under Passenger Transport by Road Class), Accommodation Service, and X-ray photography, Consultation Fee of a medical doctor, Laboratory service, among others. ***Interestingly, core inflation also slowed down on a month-on-month basis, dropping to 2.01 percent in May 2024 from 2.20 percent printed in April 2024.***

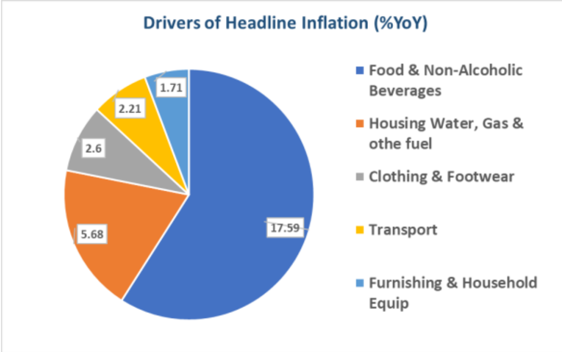
The slowing down of inflation on a month-on-month basis may suggest that recent rate hikes by the Central Bank of Nigeria are beginning to yield result. It also implies slower rise in the average prices of essential food items.

Figure 9: Year-on-Year Headline, Food and Core Inflation (May 2023 – May 2024) in per cent



Source: National Bureau of Statistics (NBS), 2024

Figure 10: Key Drivers of headline Index in May 2024



Source: National Bureau of Statistics (NBS), 2024

Price Outlook

Inflation is expected to further heighten in June 2024. Our forecast showed that inflationary pressure would heighten marginally as headline, food and core inflation are expected to rise to 34.17, 40.80 and 27.53 percent respectively.

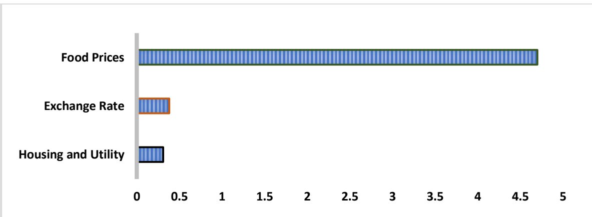
Table 1: Inflation forecast for June 2024 in Per Cent

Headline	Food	Core
34.17	40.80	27.53

Source: CAPE Economic Research and Consulting, 2024

The principal drivers shaping the forecast for headline inflation persist in food prices, the exchange rate, housing, and utility costs, contributing 4.70 percent, 0.38 percent, and 0.31 percent, respectively.

Figure 11: Driver of Predicted Inflation



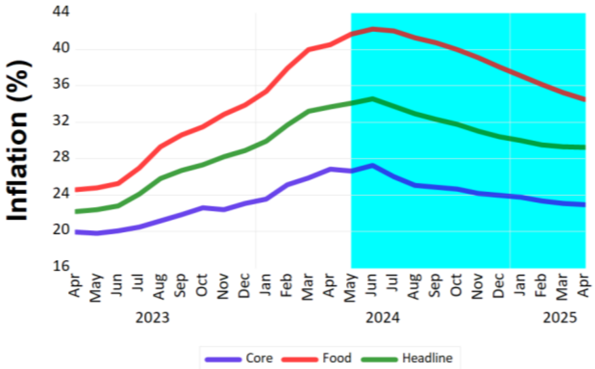
Source: CAPE Economic Research and Consulting, 2024

Our analysis underscores the significant impact of food prices, exchange rate fluctuations, and housing and utility expenses on headline inflation. Notably, the aftermath of the energy price hike and exchange rate adjustments post-deregulation in June 2023 continue to reverberate throughout the economy. These factors are anticipated to exert sustained inflationary pressure through till end June 2024.

Meanwhile, core inflation is chiefly influenced by transportation costs, education expenses, clothing prices, housing and utility charges, and healthcare expenditures. Elevated risks to inflation stem from a burgeoning fiscal deficit, the elimination of fuel subsidies, escalating exchange rate strains, and their subsequent pass-through effects on prices.

To bolster stability in the foreign exchange market, concerted efforts are imperative, necessitating fiscal authorities to complement the Central Bank's initiatives with measures aimed at attracting Foreign Direct Investment (FDI) and catalyzing exports, particularly in the oil sector initially, followed by other sectors. We anticipate that the Monetary Policy Committee (MPC) of the Central Bank of Nigeria will maintain its tight stance at its July 2024 meeting, either by holding the policy rate steady at 26.25 percent or marginally tightening it further.

Figure 12: 12-Month Inflation Projection



Source: CAPE Economic Research and Consulting, 2024

Our revised 12-month inflation outlook suggests a gradual moderation beginning in the third quarter of 2024, contingent upon prevailing conditions, with a trajectory towards more favourable levels by 2025. However, inherent risks to this projection include volatility in the exchange rate, security concerns, and policy uncertainties.

Fiscal Operations Update

The fiscal injection by the Federation Account Allocation Committee (FAAC) in June 2024, based on revenue collected in May 2024, declined by 5.4 percent to N1.143.21 trillion, compared to the N1.208 trillion distributed in May 2024. This reduced injection could help moderate inflationary pressure in June 2024 by exerting less impact on banking system liquidity. The amount distributed in June represents about 49 percent of revenue generated in May 2024 which was lower than the ₦1,208.08 billion distributed in April 2024 by ₦64.87 billion representing a decrease of 5.4 percent. The decrease was driven by the considerable drop in Import and Excise Duties, Royalty Crude and Gas, EMTL, CET Levies, and VAT. However, significant increases were recorded in Companies Income Tax Oil (CIT) and Petroleum Profit Tax (PPT) for May 2024.

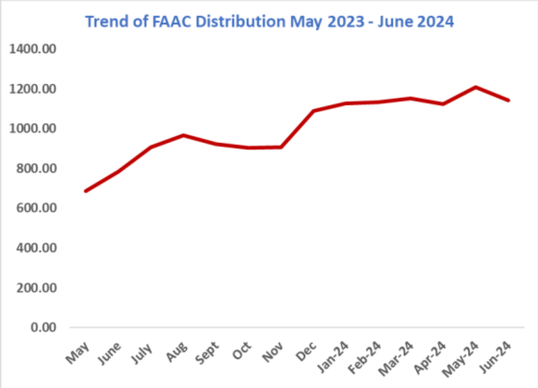
Table 2: Highlight of June 2024 FAAC Distribution (N'billion)

	June	May	% Change
Fed.	*365.81*	*390.41*	*-6.3*
State	*388.42*	*403.40*	*-3.7*
LG	*282.48*	*293.82*	*-3.9*
13%	*106.50*	*120.45*	*-11.6*
Total	**1,143.21**	**1,208.08**	***-5.4***

Source: FAAC, June 2024

Further breakdown as indicated in Table 3 showed that Federal Government received ₦365.81 billion; States, ₦388.42 billion; Local Government, ₦282.48 billion. Thirteen per cent derivation fund distributed among beneficiary states amounted to N106.50 billion. Allocations to the three tiers of government generally declined in June with Compared to May 2024. The 13 percent derivation fund distributed among oil producing states recorded a decrease of 11.6 percent. ***In a high inflation regime like the one currently experienced in Nigeria, a declining fiscal injection is expected to help decelerate inflationary pressure. However, this decline is rather too marginal to lower inflationary pressure significantly.***

Figure 13: Trend of FAAC Distribution



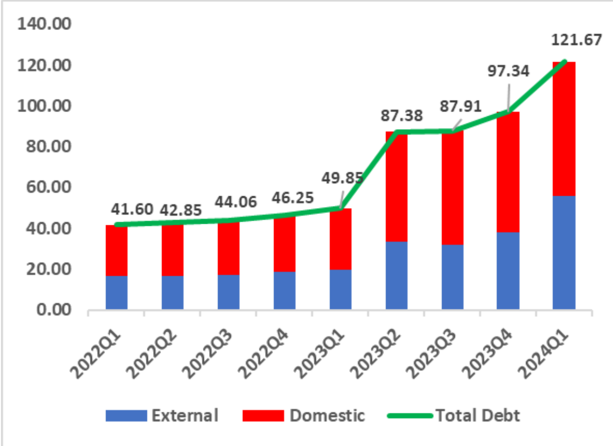
Source: FAAC, June 2024

Debt Update

Nigeria's total public debt stock maintained its upward trajectory as it surged to ₦121.67 trillion in Q12024, up from the N97.34 trillion posted in Q42023, reflecting a 24.33 percent increase. The increase was primarily attributable to exchange rate depreciation, which elevated the valuation of both new and existing debt, the securitization of Ways and Means advances, and additional borrowing to finance the deficit as stipulated in the 2024 Appropriation Act. Total domestic debt stock stood at ₦65.65 trillion (53.95 percent of total debt) while the total external debt obligations amounted to ₦56.02 trillion (46.04 percent of total debt).

At ₦121.67 trillion, Nigeria's debt-to-GDP ratio now stands at 51.2 percent, which is higher than the self-imposed threshold of 40 percent but lower than the World Bank/IMF's prudential ceiling for countries in Nigeria's peer group. Despite being within the international limit, Nigeria needs to enhance its revenue generation efforts to mitigate elevated debt sustainability risks in the near to medium term.

Figure 14:Nigeria's External and Domestic Debt Composition



Source: DMO

Conclusion

In summary, the global output growth outlook for 2024 remains cautiously optimistic yet tempered. Emerging markets face significant challenges, amplified by uncertainties and China's weak performance. Central banks' assertive measures are beginning to moderate prices in some areas, but this progress comes with trade-offs, notably affecting output and financial stability. Despite these global challenges, Nigeria's economic forecast for 2024 remains resilient, demonstrating an ability to withstand and adapt to the prevailing economic conditions.

Country in Focus – Republic of Mali

Figure 15: Economic Parameters for Republic of Mali

Source: CAPE Economic Research and Consulting, 2024