Cape Economic Performance and Prospect Bulletin – August 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 July 2024, with headline inflation rising to 34.45 percent**.*

Global Economic Update

Global economic growth is bolstered by several positive factors, including the moderation of inflation rates, more accommodative financial conditions, and a noticeable increase in global trade activity. The easing of inflationary pressures has provided relief to both consumers and businesses, reducing the cost pressures that had previously weighed on economic activity. Additionally, central banks are on the verge of more accommodative monetary policies, which are improving financial conditions by lowering borrowing costs and increasing liquidity in the financial system. The resulting pickup in global trade reflects a recovery in demand for goods and services across major economies, further contributing to the overall growth momentum.

However, despite these supportive factors, global growth rates are not projected to reach pre pandemic levels. This subdued outlook is attributed to several persistent headwinds. Elevated debt burdens, particularly in both emerging and advanced economies, constrain fiscal policy space and limit the ability of governments to stimulate growth through public spending. Higher interest rates, implemented by central banks to combat inflation, increase the cost of borrowing and can dampen investment and consumer spending. Furthermore, various geopolitical uncertainties, including trade tensions, political instability, and conflicts, create an unpredictable global environment that can disrupt economic activity and undermine business confidence. Consequently, global output growth for 2024 is forecast at 2.9 percent, marginally down from 3.1 percent in 2023.

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.

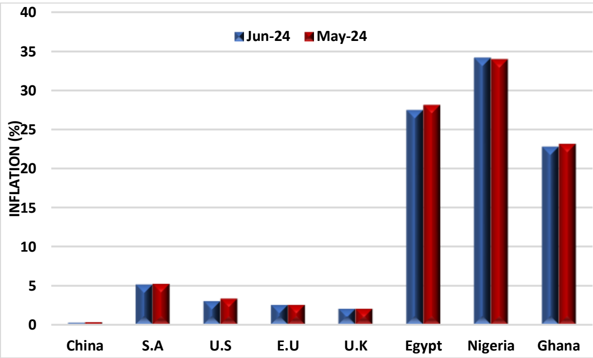
Emerging markets are anticipated to outpace the growth of advanced economies. China's economic expansion is projected to remain positive in 2024, driven by increased investment despite challenges from the persistent underperformance of the real estate sector and weak household spending. Other emerging economies, such as India, Indonesia, Vietnam, and the Philippines, are on track to be among the fastest-growing economies, bolstered by strong domestic consumption and substantial foreign investments. In contrast, key Latin American emerging markets, including Mexico and Brazil, may face growth constraints due to slower domestic and international demand, fiscal consolidation measures, and strict monetary policies implemented to combat inflationary pressures.

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

Global inflationary patterns remain diverse, with households experiencing persistent financial strain despite widespread hawkish monetary policies. Geopolitical unrest, notably the Israel-Hamas conflict and the ongoing military engagement between Russia and Ukraine, exacerbates inflationary pressures by significantly impacting commodity prices such as oil and grains. Additionally, climate change concerns affecting global logistics may undermine supply chains. The effectiveness of policy rate hikes in curbing inflation varies between developed and emerging markets. Particularly concerning is the risk of gain reversal in the already declining inflation trend in some advanced economies, hence the prolonged hold stance of monetary policy and the hesitation in commencement of a loosening as seen in the United States. A few economies like the UK have achieved the 2 percent target, however it remains cautious. While, in the Euro area, although it has not achieved its target rate loosening pressure continue to mount.

Similarly, while the pressure to loosen monetary policy is not intense—given the need to remain competitive to attract capital inflows—inflation has begun to moderate in most emerging economies. However, a few outliers, such as Nigeria, continue to experience heightened inflationary pressures. In Nigeria's case, this is largely due to bold government reforms and their resultant effects. These reforms, while necessary for long-term economic stability, have contributed to short-term inflationary spikes, contrasting with the broader trend of inflation moderation observed in other emerging markets.

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



Source: Various National Statistics Offices

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. Specifically, the Fed Beige Book showed slowing growth and a loosening labour market, as inflation was declining which is supporting evidence for a September interest rate cut by the Fed. 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 July 2024, equities market reached sustained its 2024 rally mostly for the first half of the month. However, from July 17, 2024, market perceptions changed, with reallocation to small caps from large caps, especially in Information Technology. The S&P 500® was up 1.13 percent in July, bringing its Year-to-date return to 15.78 percent. The Dow Jones Industrial Average® increased 4.41 percent for the month and was up 8.37 percent Year-to-date. The S&P MidCap 400® gained 5.73 percent for the month, bringing its Year-to-date return to 11.38 percent. The S&P SmallCap 600® added 10.71 percent in July and turned positive, up 8.92 percent Year-to-date.

In the fixed income market, government bond yields continued to decline, with shorter-dated bonds showing the most noticeable movement. In the US, June's soft Consumer Price Index (CPI) data and a weakening labour market have heightened investor expectations for Federal Reserve rate cuts in 2024 and 2025. This optimism boosted US Treasuries, which gained 2.2% over the month. The rally at the front end of the yield curve also caused the yield curve to steepen, with the spread between the 10-year and 2-year US Treasury yields narrowing to -21 basis points, the smallest gap since January 2024. In the UK, stronger-than-expected GDP growth in the second quarter, coupled with persistent inflation in the services sector, suggests that interest rate cuts may proceed more gradually compared to the US and Europe. Consequently, UK underperformed, returning only 1.9% over the month. In the eurozone, government bonds in peripheral countries continue to outperform core bonds as investors seek higher yields in anticipation of further European Central Bank interest rate cuts. Overall, July was a volatile month in the markets. Softer inflation and labour market data from the

US heightened expectations of rate cuts, spurring a rotation into small-cap stocks and other interest-rate-sensitive asset classes.

In the currency market, several major currencies strengthened against the US dollar. The dollar index, which measures the greenback's performance against a basket of currencies including the yen and the euro, recorded a modest increase of 0.07 percent, reaching a level of 102.94. Specifically, the US dollar appreciated by 0.4 percent against the Japanese yen, bringing the exchange rate to 144.74 yen per dollar. Conversely, the euro experienced a slight depreciation, declining by 0.2 percent to an exchange rate of US$1.093. The expectation of policy loosening by the Federal Reserve is likely to further weaken the U.S. dollar compared to other principal currencies, but not drastically.

In the commodities market, gold prices remained largely stable and improved to around US$2,448 per ounce. The expected rate cuts by the Federal Reserve, may catalyse 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 July 2024 experienced volatility and a downward price adjustment due to various economic and geopolitical factors. Consequently, crude oil prices experienced a moderation, with WTI ending at US$78.48 per barrel and Brent at US$81.54. 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 is expected to further slowdown 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, following the outcome of the general elections, output growth is expected to expand, and sustained stable inflation is expected to trigger rate cuts.

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 market, we anticipate sustained volatility, as there is a risk that bond markets may have moved too quickly. The extent of policy easing implied by current market pricing seems unlikely without a recession. Given this, we remain cautious about sustained small-cap outperformance. Instead, we continue to focus on more regionally diversified exposures. Stronger economic momentum and more attractive valuations can be found in areas such as the UK and continental Europe, providing the additional benefit of some diversification against US market and political risks. Furthermore, we anticipate a further shift of portfolio flows into emerging markets 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.

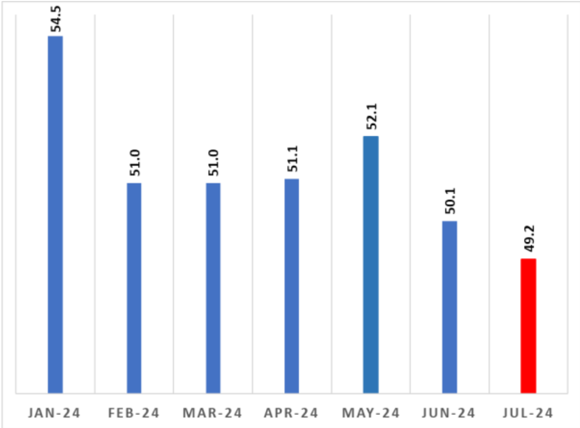
In the commodity market, oil prices are expected to be encumbered in the latter half of 2024 as OPEC+ scales back production cuts. Natural gas and coal prices are projected to drop due to ample supply and high inventory levels. Industrial metal prices are likely to rise driven by China's easing of fiscal 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 private sector output growth in the first month of the Q32024 kicked-off on a weak note on account of elevated inflationary pressures which dampened customers' demand, leading to deterioration of business activity and new orders in July 2024. The Stanbic IBTC headline PMI for July 2024 dipped to 49.2 points from the June print of 50.1 points, representing its lowest level in eight months and the first sub-50 reading in 2024. For guidance, a PMI reading above 50.0 signals an improvement in business conditions, while readings below 50.0 indicates a worsening business condition, while a PMI of 50 points represents a no-change benchmark. Stanbic IBTC PMI figure for July 2024 clearly indicates a contraction in private sector economic activities attributed to surging input costs, particularly, raw materials and energy, increased staff costs, worsening exchange rate among others, compelled businesses to raise their selling prices. Increased prices led to the reduction in customers' purchasing power and consequently, lower consumer demand. As expected, output and new orders declined on the back on low demand.

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

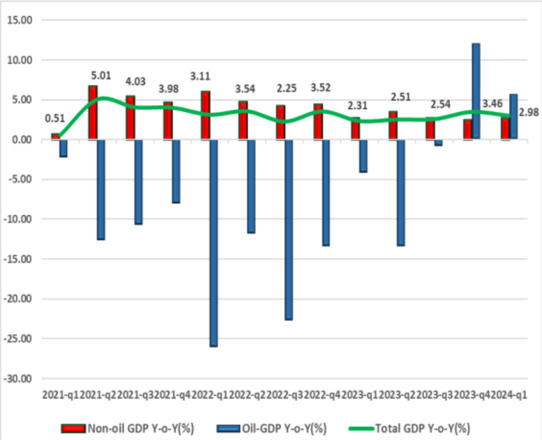


Source: Stanbic IBTC

More than ever, output growth has become paramount in Nigeria amid the ongoing nationwide hunger protest. The public discontent in Nigeria underscores the urgent need for strategies that promote output growth and put food on the table of the common man at affordable prices. This can be achieved by focusing on policies that enhance productivity, support industrial development, and stabilize the economy.

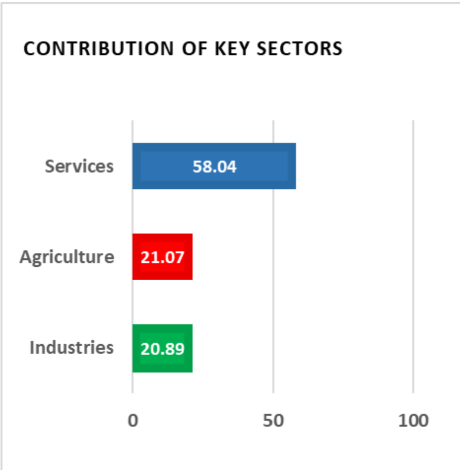
Specifically, effective policy responses are required to the achieve a balance between output growth and inflation thereby keeping the economy on the path of sustainable recovery. The government needs to judiciously implement the recent fiscal initiatives aimed at curbing inflation such as suspension of import duties on essential staple food items, raw materials and other direct inputs used for manufacturing, inputs for agriculture production including fertilisers, seedlings, and chemicals. This would enable businesses enjoy lower input costs. On the monetary policy side, the Central Bank of Nigeria would need to continue to slow down on its aggressive rate hikes as we enter into harvest season when inflation is inherently expected decelerate.

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



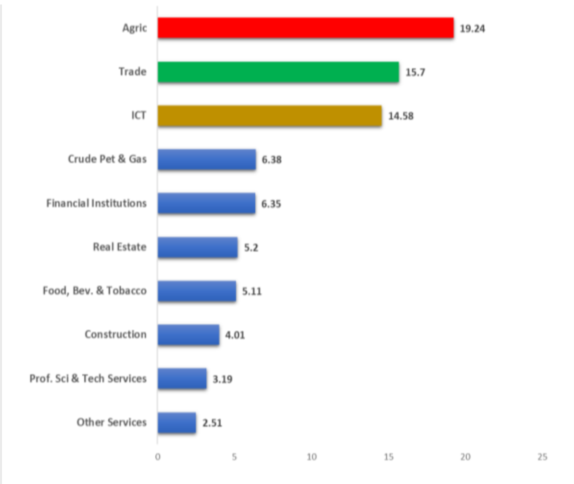
Source: National Bureau of Statistics (NBS)

Figure 4: Sectoral Contribution to GDP in Q12024



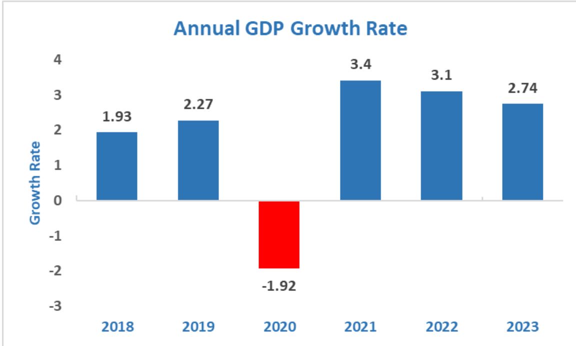
Source: National Bureau of Statistics (NBS)

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

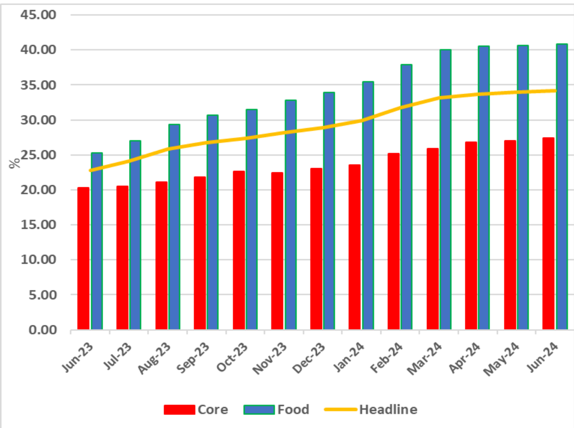
Nigeria's headline inflation rose to a 28-year high in June 2024 on account of rising costs of inputs, exchange rate deterioration, insecurity, infrastructural deficit among other bottlenecks. Headline inflation hit 34.19 percent in June 2024, rising by 0.24 percentage points above the 33.95 percent printed in May 2024. On a year-on-year basis, the headline inflation rate in June 2024 was 11.40 percentage points higher than the 22.79

percent recorded in June 2023. This indicates a significant increase in the headline inflation rate for June 2024 compared to the same month in the previous year. This was driven mainly by the increases in the prices of food and ono-alcoholic beverages (Figure 10). On a month-on-month basis, the headline inflation rate rose to 2.31 percent, marking an increase of 0.17 percentage points from the 2.14 percent recorded in May 2024. This indicates that the rate at which price level increased in June 2024 was higher when compared to that of May 2024.

Food inflation rate reached a new peak of 40.87 percent in June 2024 from the 40.66 percent printed in the month of May. On a year-on-year basis, it was elevated by 15.62 percentage points from the 25.25 percent recorded in June 2023, mainly driven by the prices of millet whole grain, garri, guinea corn, yam, coco yam, groundnut oil, palm oil, among others. On a month-on-month basis, the food inflation rate in June 2024 was 2.55 percent, reflecting a 0.26 percentage points increase from the 2.28 percent in May 2024.

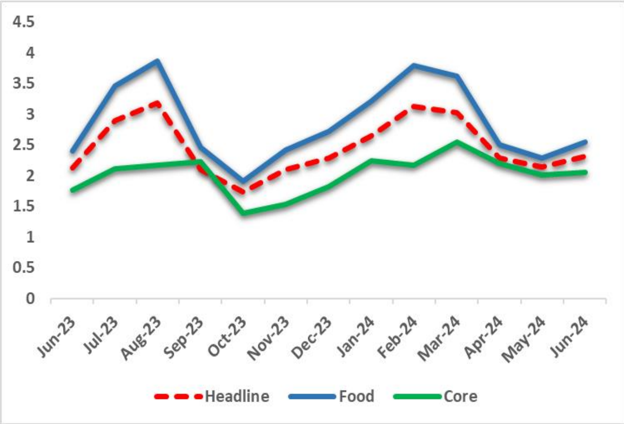
Similarly, core inflation rose to 27.40 percent in June 2024, from the 20.27 percent and 27.04 percent recorded in June 2023 and May 2024, respectively. On a month-on-month basis, core inflation rate increased by 0.05 percent to 2.06 percent in June 2024 compared to May 2024 when it stood at 2.01 percent.

Figure 7: Year-on-Year Headline, Food and Core Inflation (June 2023 – June 2024) in per cent



Source: National Bureau of Statistics (NBS), 2024

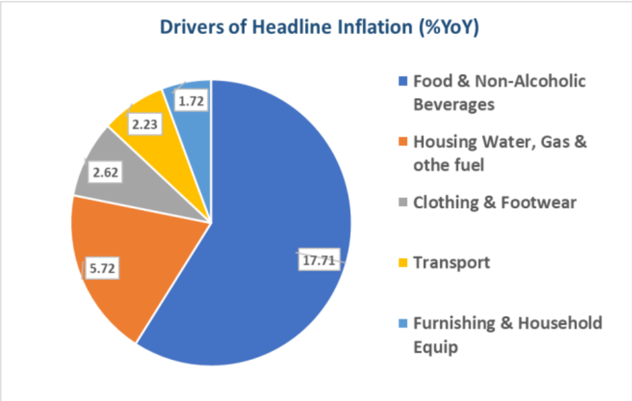
Figure 8: Month-on-Month Inflation Rates (June 2023 – June 2024) in percent



Source: National Bureau of Statistics (NBS), 2024

The elevation of month-on-month inflation measures suggest that inflation generally accelerated in June 2024 inspite of the continuous rate hike by the Central Bank of Nigeria.

Figure 9: Key Drivers of headline Index in June 2024



Source: National Bureau of Statistics (NBS), 2024

Price Outlook

Inflation is expected to further heighten in July 2024. Our forecast showed that inflationary pressure would heighten marginally as headline, food and core inflation are expected to rise to 34.45, 41.30 and 27.63 percent respectively.

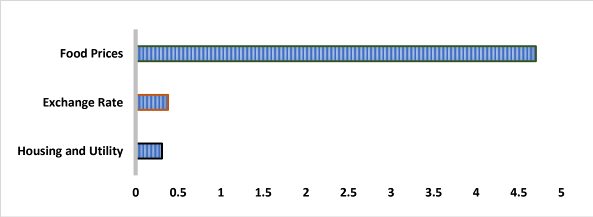
Table 2: Inflation forecast for July 2024 in Per Cent

Headline	Food	Core
34.45	41.30	27.63

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 10: Driver of Predicted Inflation



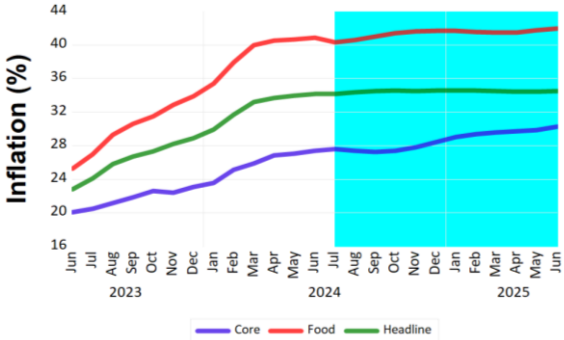
Source: CAPE Economic Research and Consulting, 2024

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 continue to reverberate throughout the economy. These factors are anticipated to continue to exert sustained inflationary pressure.

Meanwhile, core inflation is principally 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.

As we opined in our previous release the Monetary Policy Committee (MPC) of the Central Bank of Nigeria maintained its tight stance at its July 2024 meeting with a marginal hike of 50 basis points, shifting the policy rate to 26.75 percent. This remained premised on the need to achieve price stability and equally remain competitive in the foreign Portfolio Investment (FPI) market. 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 catalysing 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 September 2024 meeting, either by holding the policy rate steady at 26.50 percent or marginally tightening it further.

Figure 11: 12-Month Inflation Projection



Source: CAPE Economic Research and Consulting, 2024

Our revised 12-month inflation outlook suggests a plateauing of inflation for the rest of 2024 going into 2025, contingent upon prevailing conditions. However, inherent risks to this projection include volatility in the exchange rate, security concerns, and policy uncertainties.

Fiscal Operations Update

The fiscal injection from the Federation Account Allocation Committee (FAAC) in July 2024, for revenue collected in the month of June 2024, increased by 18.5 percent to N1.354.38 trillion, compared to the N1.143.21 trillion distributed in June 2024. The increase in fiscal injection could further heighten inflationary pressure in July 2024 as it impacts on banking system liquidity. The amount distributed in July represents about 54.5 percent of total revenue collected, which was higher than the amount distributed in June 2024 by ₦211.17 billion representing a decrease of 18.5 percent. The increase was driven by the significant rise companies' income tax (CIT), VAT, Import and Excise Duties and EMTL.

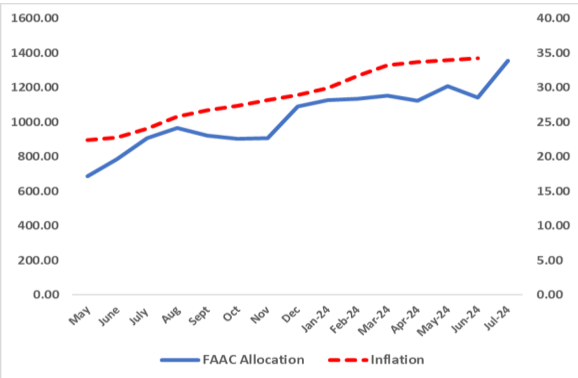
Table 3: Highlight of July 2024 FAAC Distribution (N'billion)

	June	June	% Change
Fed.	*459.78*	*365.81*	*25.7*
State	*461.98*	*388.42*	*18.9*
LG	*337.02*	*282.48*	*19.3*
13%	*95.60*	*106.50*	*-10.2*
Total	**1,354.38**	**1,143.21**	***18.5***

Source: FAAC, July 2024

Further breakdown as indicated in Table 3 showed that Federal Government received ₦459.78 billion; States, ₦461.98 billion; Local Government, ₦337.02 billion. Thirteen per cent derivation fund distributed among beneficiary states amounted to N95.60 billion. Allocations to the three tiers of government generally increased in June with compared to June 2024. The 13 percent derivation fund distributed among oil producing states decreased of 10.2 percent. ***In an environment characterised by high inflation, such as the one currently facing Nigeria, additional fiscal injection is likely to exacerbate inflationary pressures. When the government increases spending without a corresponding increase in productivity, it boosts aggregate demand in the economy. This surge in demand can lead to a further escalation in price levels as supply struggles to keep pace. Consequently, the inflationary spiral intensifies, complicating efforts to stabilize prices and undermining the purchasing power of the currency.***

Figure 12: Trend of FAAC Distribution and Inflation Rate in Nigeria



Source: FAAC, July 2024

Assessing the Economic Implications of the ₦6.2 trillion 2024 Supplementary Budget

The President presented a supplementary budget of ₦6.2 trillion to the National Assembly, following an amendment to the 2024 Appropriation Act and the 2023 Finance Act. This would bring the total 2024 budget to ₦35.55 trillion. The amendment seeks to amend the principal Act to provide the sum of N3.2 trillion for Renewed Hope infrastructure projects and other critical infrastructure projects to be undertaken across the country and the sum of N3 trillion to fund recurrent expenditure, mainly, the newly approved minimum wage of N70,000. The supplementary budget will be partly funded by the windfall tax imposed on Nigerian banks for their exchange rate revaluation gains in 2023.

The introduction of the supplementary budget is expected to intensify inflationary pressures by boosting aggregate demand. This scenario will likely prompt the Central Bank of Nigeria to maintain or even tighten its monetary policy stance to control rising inflation, resulting in elevated interest rates throughout the latter half of 2024. Prolonged high-interest rates may discourage private sector borrowing, potentially hindering economic recovery and growth. Therefore, the government must carefully manage the scale of its fiscal expansion to avoid excessive inflation, which could destabilize monetary policy and economic stability.

Furthermore, the supplementary budget may lead to a larger fiscal deficit, necessitating additional borrowings which will likely drive interest rates higher, thereby, further complicating Nigeria's debt sustainability. It is therefore crucial to exercise prudent fiscal management to prevent unsustainable debt accumulation that could threaten long-term economic stability in Nigeria.

Conclusion

In summary, the global output growth outlook for 2024 remains cautiously optimistic but tempered by various challenges. Emerging markets, in particular, are grappling with significant hurdles, exacerbated by uncertainties and China's weak performance. Central banks' assertive monetary measures are starting to moderate inflation in some regions, but this progress is not without trade-offs, notably impacting economic output and financial stability. Despite these global challenges, Nigeria's economic forecast for 2024 remains resilient, demonstrating a robust capacity to withstand and adapt to prevailing economic conditions.

Country in Focus – Republic of Burkina Faso

Figure 13: Economic Parameters for Republic of Burkina Faso

Source: CAPE Economic Research and Consulting, 2024