Michael Famoroti *
m.famoroti@vetiva.com

December Inflation

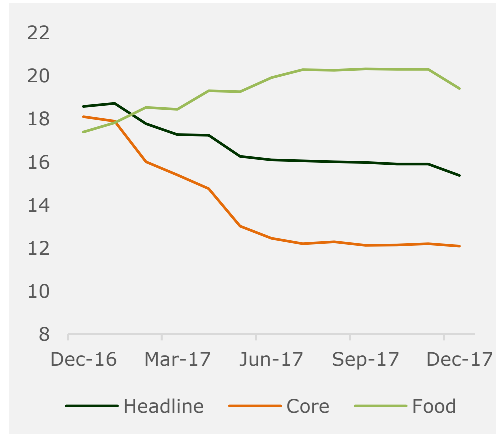
Year-end inflation offers hope for 2018

Economic Research
18 January, 2017

December Inflation came in below Vetiva and Consensus expectation of 15.7% y/y and 15.8% respectively, registering at 15.4% y/y (November: 15.9% y/y) despite nationwide fuel shortages that increased average premium motor spirit (PMS) prices by 18% in the month. The decline in inflation at year-end is most markedly seen in the m/m inflation print – from 0.78% to 0.59% – which is the lowest since October 2015 and compares to a FY'17 average of 1.20%. Across the sub-indices, Food Inflation and Core Inflation moderated from 20.3% y/y and 12.2% y/y to 19.4% y/y and 12.1% y/y respectively.

Food prices, the pressure point for most of 2017 (up 200bps from December 2016 to December 2017) have calmed in recent months, supporting the view of relative food price stability in 2018. Though up y/y (15.8% to 15.9%), Imported Food Inflation moderated from 1.24% to 1.12% m/m, a notable improvement from previous levels (prior 4-month average: 1.28%) and in line with the trend of declining global food prices – FAO index down 3% m/m in December.

Inflation Trend (%)

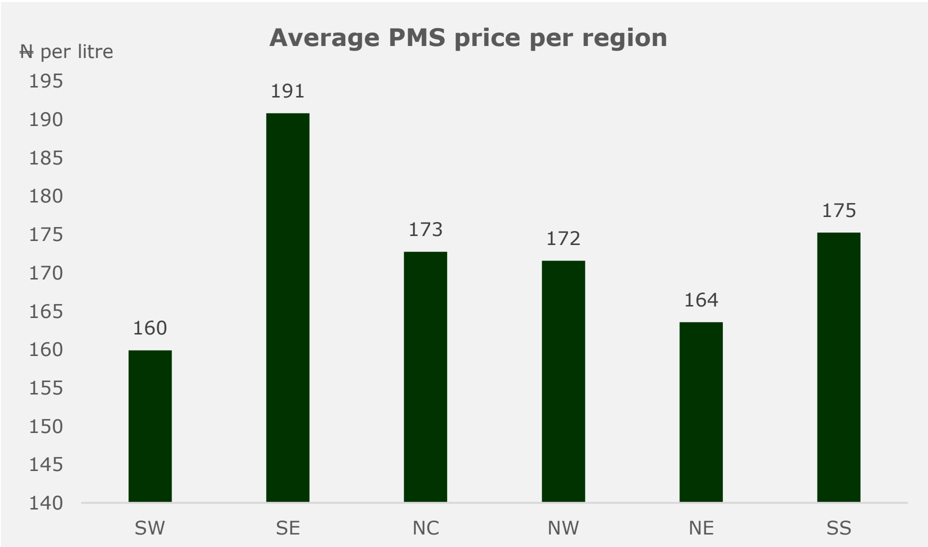


Source: NBS, Vetiva Research

High crude oil prices are bad news for petroleum products

In our November Inflation note "*Inflation Déjà vu in November*", we highlighted that "Amidst recent higher oil prices, disruptions in getting refined products to the depots has exerted pressure on the price charged by the depots and this, in turn, is pressuring the pump price. Amidst strike threats by petroleum marketers and queues building up, we see a greater risk of black markets for the product in the interim". Unsurprisingly, PMS prices spiked during the month, surging to an average of ₦171.79 per litre, the highest on record. Price pressure was most keenly felt in the South-East region of the country where prices averaged ₦190.90 per litre. In addition, kerosene and diesel prices were also up m/m – 6% and 3% respectively – as higher global crude oil prices squeezed importers. We note that the petroleum product price spike did not materially affect Core Inflation in December, with the only notable uptick coming in Transport Inflation which increased m/m from 0.78% to 0.91%. With oil prices still above $60/bbl (December average: $64/bbl, Ytd average: $69/bbl), landing cost of petroleum products remain high, discouraging importation and pressuring the retail price of these products. Whilst we expect continued pass-through to kerosene and diesel prices despite NNPC intervention, we expect a more muted price response for PMS. Specifically, we do not envisage that there will be a price revision or deregulation given the proximity of elections. Rather, we anticipate either a continuation of the current regime where NNPC imports and distributes to marketers or the introduction of an implicit foreign exchange subsidy. However, we note that the persistence of the status quo would likely mean intermittent product shortages during the year – as long as oil prices remain strong – and some pass-through to the realized retail price like we saw in December.

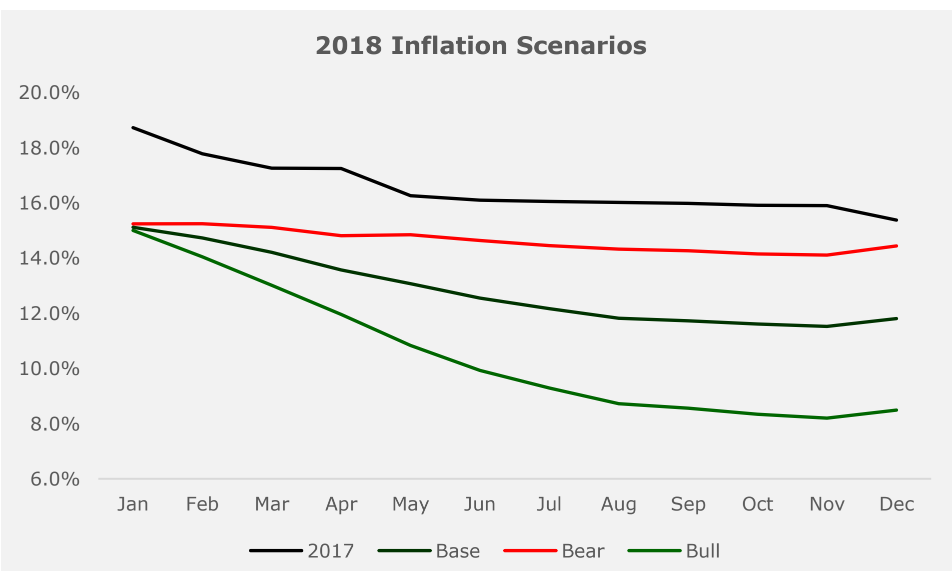
Inflation is calculated by looking at corresponding numbers of the Consumer Price Index (CPI). The CPI is a measure that examines the weighted average of prices of a basket of consumer goods and services over time, relative to a base year. The current base year for the Nigerian CPI is 2009. Annual inflation for a month is computed by comparing the percentage change in the CPI figure for that month in the two comparison years.



Source: NBS, Vetiva Research

Out of the woods?

Nigeria's inflation averaged 15.6% and 16.5% in 2016 and 2017 respectively, rising from 9.6% in January 2016, peaking at 18.7% a year later and now settling at 15.4% in December 2017. We hold the view that we are journeying out of the woods in terms of inflation. In 2018, we anticipate relative stability in domestic food prices and in the exchange rate, whilst we consider significant revisions to PMS prices or a hike in the minimum wage as unlikely over the next 12 months. However, we still expect some pass-through from higher energy prices as well as some inflationary effect of election spending in late 2018. With base effects from high 2017 inflation kicking in, we forecast average inflation of 12.8% in 2018 – with inflation moderating over the course of the year from 15.1% y/y in January 2018.



Source: Vetiva Research

Disclosures Section

Analyst Certification
The research analyst(s) denoted by an "*" on the cover of this report certifies (or, where multiple research analysts are primarily responsible for this report, the research analysts denoted by an "*" on the cover or within the document individually certifies, with respect to each security or issuer that the research analyst(s) cover in this research) that: (1) all of the views expressed in this report accurately articulate the research analyst(s) independent views/opinions, based on public information regarding the companies, securities, industries or markets discussed in this report. (2) The research analyst(s) compensation or remuneration is in no way connected (either directly or indirectly) to the specific recommendations, estimates or opinions expressed in this report.

Analysts' Compensation
The research analyst(s) responsible for the preparation of this report receive compensation based upon various factors, including the quality and accuracy of research, client feedback, competitive factors, and overall firm revenues, which include revenues from, among other business units, Investment Banking and Wealth Management.

Frequency of Next Update
An update of our view would be provided when next there are substantial developments/financial news on the company.

Conflict of Interest
It is the policy of Vetiva Capital Management Limited and its subsidiaries and affiliates (individually and collectively referred to as "Vetiva") that research analysts may not be involved in activities that suggest that they are representing the interests of Vetiva in a way likely to appear to be inconsistent with providing independent investment research. In addition, research analysts' reporting lines are structured so as to avoid any conflict of interests. For example, research analysts are not subject to the supervision or control of anyone in Vetiva's Investment Banking or Sales and Trading departments. However, such sales and trading departments may trade, as principal, on the basis of the research analyst's published research. Therefore, the proprietary interests of those Sales and Trading departments may conflict with your interests.

Important Regional Disclosures
The analyst(s) involved in the preparation of this report may not have visited the material operations of the subject Company (ies) within the past 12 months. Commission is the commission rate or the amount agreed with a customer when setting up an account or at any time after that. To the extent this is a report authored in whole or in part by a Non-U.S. analyst and is made available in the U.S., the following are important disclosures regarding any Non-U.S. analyst contributors: The Non-U.S. research analysts (denoted by an * in the report) are not registered/qualified as research analysts with FINRA; and therefore, may not be subject to the NASD Rule 2711 and NYSE Rule 472 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account. Each analyst (denoted by an *) is a Non-U.S. Analyst and is currently employed by Vetiva.
Legal Entities
Vetiva Capital Management Limited (VCML) is an Ordinary Member of the Nigerian Stock Exchange (NSE) and is registered with the Nigerian Securities & Exchange Commission (SEC) to conduct Issuing House and Financial Advisory business. Through its subsidiaries duly licensed and regulated by the SEC, VCML also carries on the business of Fund/Portfolio Management, Brokerage & Dealing (on both the NSE and the NASD OTC), Market Making and Trusteeship.

General
This research report is based on public information which the research analyst(s) consider credible and reliable. Facts and views presented in this material have not been reviewed by, and may not reflect information known to, professionals in other business areas of Vetiva, including the Investment Banking team and the Wealth Management team, as Vetiva has established information barriers between its Research team and certain business groups. Whilst reasonable care has been taken in preparing this report, no responsibility or liability is accepted either by Vetiva, its officers or any of its employees for any error of fact or opinion expressed herein. No reliance should be placed on the accuracy, fairness or completeness of the information contained in this report as it has not been verified by the research analyst(s) involved or the companies whose securities have been referred to except as otherwise disclosed. Neither Vetiva nor any of its officers or employees including the research analyst(s) warrant or represent the accuracy or completeness of information set out in this report.

Any ratings, forecasts, estimates and opinions set forth in this report constitute the analyst(s) position as at the date and time of this report and may not necessarily be so after the report date and time, as they are subject to change without notice. It is also instructive to note that a company's past performance is not necessarily indicative of its future performance as estimates are based on assumptions that may or may not be realized.

The value, price or income from investments mentioned in this report may fall, as well as rise, due to economic conditions, industry cycles, market indices, operational or financial conditions of companies or other factors. Thus, Vetiva and its officers and employees shall not accept liability for any loss arising from the use of this report or its contents in making investment decisions or recommendations. This report provides general information only.

It is not intended to provide personal investment advice and does not take into account the specific investment objectives, financial situation and the particular needs of any specific person. Investments and securities discussed in this report may not be suitable for all investors and certain investors may not be eligible to purchase or participate in some or all of them. Users of this research report should independently determine the suitability and evaluate the investment risks associated with investments and securities discussed in this report. All investors are solely responsible for their investment decisions. Any decision to purchase or subscribe for securities in any offering must be based solely on existing public information on such security or the information in the prospectus or other offering document issued in connection with such offering, and not on this report. Vetiva, through business units other than Vetiva Research, may have issued and may in the future issue trading ideas or recommendations that are inconsistent with, and reach different conclusions from, the information presented in this report.

Such ideas or recommendations reflect the different time frames, assumptions, views and analytical methods of the persons who prepared them, and Vetiva is under no obligation to ensure that such other trading ideas or recommendations are brought to the attention of any recipient of this report. Vetiva may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report. To the extent that this report discusses any legal proceeding or issue, it has not been prepared as nor is it intended to express any legal conclusion, opinion or advice. Information relating to the tax status of companies whose securities are discussed in this report is not intended to provide tax advice or to be used by anyone to provide tax advice.

By accepting and making use of this research report, you agree to be bound by the foregoing limitations.

No portion of this document may be reprinted, sold or redistributed without the written consent of Vetiva Capital Management Limited. Vetiva research report is disseminated and available primarily electronically, and, in some cases, in printed form.

Additional information on recommended securities/instruments is available on request.