KPMG Financial Service Industry (FSI) Pulse

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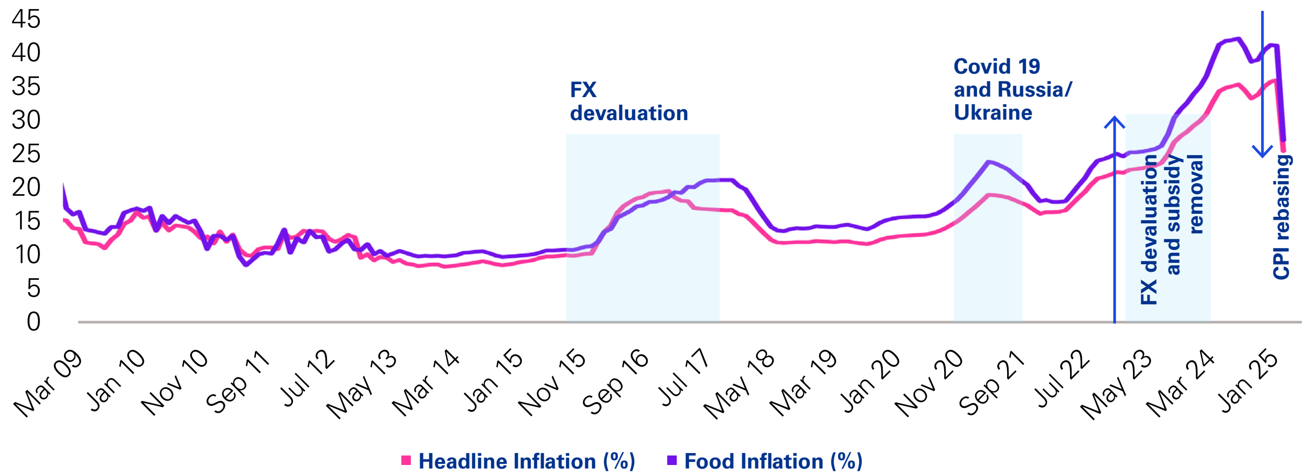
Nigeria's Consumer Price Index (CPI) Rebasing: A Boon or a Blow for Financial Markets?

Nigeria's financial landscape could be bracing for a major shift. The country's headline and food inflation came in at 24.48% and 26.08%, respectively, in January 2025 after the much-awaited rebasing of the CPI by the National Bureau of Statistics (NBS).

These new technically adjusted figures are in stark contrast to the all-time highs of 34.80% recorded for headline inflation and 39.84% reported for food inflation in December 2024 under the old methodology with 2009 as the base year, making relative comparison nearly impossible as the basis of computation is materially different.



The revised estimates reflect changes in the following areas:

Base year

Change in the base year from 2009 to 2024

Rebasing

Consumption basket

Increase in the number of items in the consumption basket from the current 740 items to 960 items

Expansion

Weights

Adjusted weights with a lower weight for high-inflation items like food and non-alcoholic beverages (from 51.8% to 40.1%) and higher weights for transport (6.5% to 10.7%), health (from 3.0% to 6.1%), and restaurant & accommodation services (from 1.2% to 12.9%)

Re-weighting

Inflation indices

Introduction of three additional indices -Services index, Energy index, and Farm produce index

Disaggregation

Implications for the financial sector

The technical adjustment to the CPI led to a major downward adjustment to Nigeria's inflation figures. While these new inflation numbers only reflect a change in the underlying methodology, they still carry implications for the financial sector from a policy, market reaction and investors sentiments standpoint.

1 Monetary policy recalibration

The commitment of the Central Bank of Nigeria (CBN) to an inflation-targeting framework means that the technically adjusted inflation rate of 24.48% is now closer to the apex bank's target of 21.4% earlier set for 2024, setting the tone for the CBN to reconsider its current stance on monetary policy.

Meanwhile, the scale of the last increase in MPR (+25bps and lowest in 2024) already signalled an imminent peaking of rate hikes by the CBN. This is apart from mounting pressures from the real sector for lower interest rates amidst discontent over high interest expenses.

Thus, we see the apex bank changing gear to a more relaxed monetary policy soon after initially pausing on rates hikes, if it considers the technically adjusted inflation figures as more reflective of inflation dynamics. The gradual pivot to a dovish monetary policy is expected to provide the much-needed wiggle room to support economic growth.

2 Banking Industry

Banks may benefit from improving liquidity conditions as credit demand increases across various sectors while also experiencing reduced risks of non-performing loans (NPLs) correlated with high interest rates. However, interest income of banks would be significantly impacted once rates moderate. The current level of profits declared by banks could reduce. Consequently, banks will need to reassess their credit risks, loan pricing, and asset allocation strategies.

3 Insurance Industry

Insurance companies, which largely depend on investment income, will need to rethink their strategies and adjust their investment portfolios as the economy braces for a lower interest rate environment. Also, because inflation plays a crucial role in determining risk and premiums, the impact of a major fall in the revised inflation figures will also trickle down to the pricing of insurance products.

4 Pension Industry

In the pension industry, the lower inflation and a potential shift in CBN policy will not only affect the valuation of pension liabilities but also require fund managers to rebalance their portfolios to optimize returns in the evolving economic landscape.

5 Capital Market

Lower inflation and potential interest rate cuts may drive stock prices up by making equities more attractive to both domestic and foreign investors. We also expect the yield curve to respond to the interest rate outlook following the CPI rebasing.

Beyond Rebasing: Addressing Structural Inflation Drivers

In line with global leading practices, the case for rebasing the CPI is compelling considering the need to capture current economic realities, better reflect consumers' shifting expenditure patterns, and support the development of targeted policies. We anticipate that the exercise would provide the space for monetary policy to start easing to support growth after a temporary wait-and-see posture by the apex banks.

However, while the rebasing of the CPI is a critical step, it is also important to address the structural drivers of inflationary pressures from a fiscal policy standpoint. Current initiatives such as those targeted at boosting agricultural productivity and closing infrastructural gaps must be accelerated. Transportation and logistics bottlenecks contributing to supply chain inefficiencies should be moved to the front burner while also strategically addressing insecurity.

Long-term initiatives should also focus on diversifying the economy to boost foreign exchange earnings from non-oil sources. These fiscal initiatives will be crucial for achieving a stable macroeconomic environment that will catalyze sustainable growth and development.

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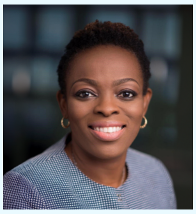

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