

Flashnotes

Issue 10 | 17 July 2023 | KPMG in Nigeria

Subsidy Removal Muted Impact on Inflation in June 2023

Highlights

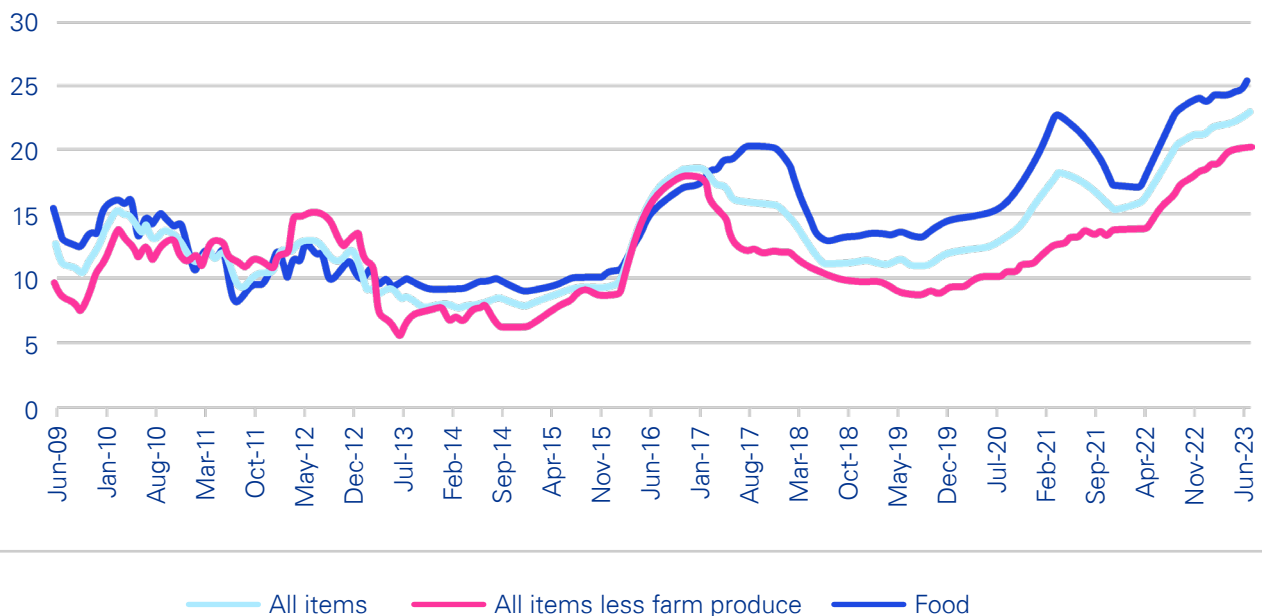
- Inflation rises only slightly to a new high of 22.79% in June 2023 from 22.41% in May 2023.
- Data reveals a surprising and unexplained limited impact of subsidy removal on headline and month on month inflation and on transport and energy inflation for June 2023.
- While there is no clear explanation for the seemingly muted effect of the subsidy removal policy on inflation and explanations at this time to suggest a time lag in policy effect, we will wait till the CPI is released for July 2023 to take a further review.

Event

In June 2023, the headline consumer price index (CPI) increased on a year-on-year basis from 22.41% in May 2023 to 22.79%. On a monthly basis, following the third consecutive increase recorded in May 2023, the CPI rose further from 1.94% to 2.13% in June 2023 which is 0.67% lower than the highest in two-decade recorded in May 2016.

Both the core and food components of inflation increased to 20.27% and 25.25% in June 2023 on a year-on-year basis respectively accounting for 0.21% and 0.43% addition from the previous month values of 20.06% and 24.82%. On a monthly basis, while food prices increased to 2.40% in June 2023 from 2.19% in May 2023, core inflation declined from 1.81% in May 2023 to 1.74% in June 2023.

Inflation: Composite Year on Change (%)

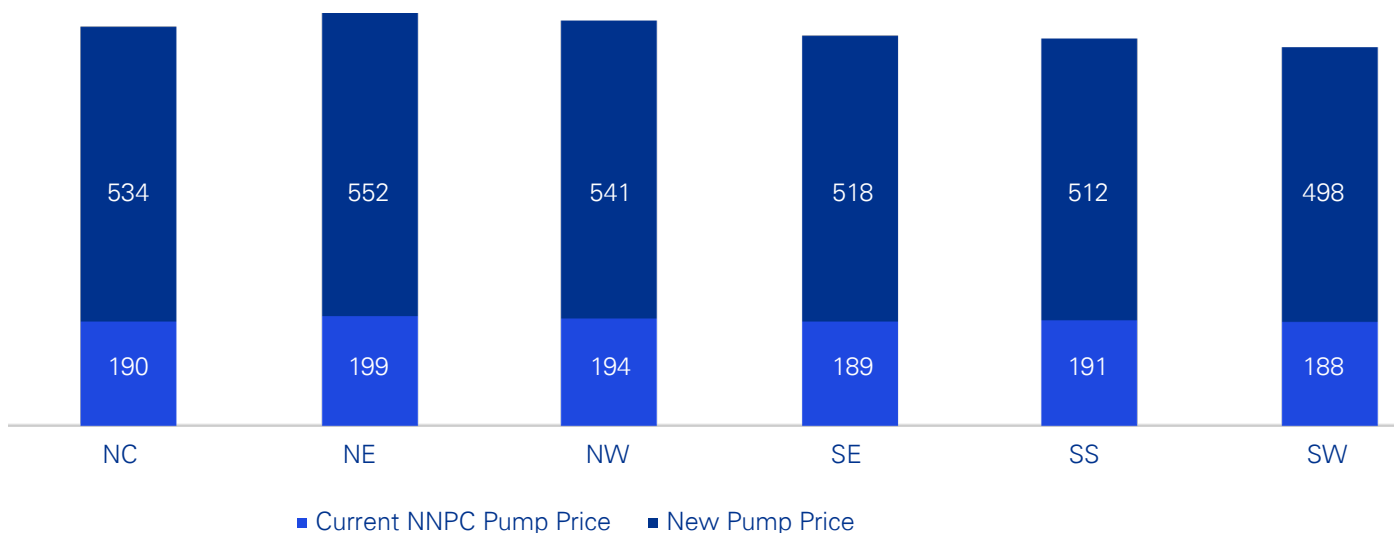


Analysis/Opinion

The evidently muted impact of the removal of fuel subsidies and application of a VAT on diesel imports in the presence of a liberalised FX regime all of which came in the period under review will catch most analysts and policy makers by surprise. Our expectation was for an increase between 25-30%.

Following the adjustment of pump prices in early June by almost 200% on average, households and businesses have expressed concerns about rising food and transportation costs and its impact on eroding households purchasing power.

Average Current & New Pump Price



Policy makers have also expressed similar concerns and encouraged consumers and businesses to bear the challenges while at the same time set up committees to work on interventions to cushion the inflationary impact of the reforms especially the subsidy removal on consumers. In this regard, the president recently requested National Assembly authorisation to borrow N500 billion in addition to the \$800 million earlier provided by the World bank aimed at providing palliative support to consumers. At the same time some businesses have reviewed workers' salaries upwards while some State governments have introduced fewer working days all aimed at reducing the inflationary burden on workers income.

The effect of the policy on inflation which contradicts anecdotal evidence in the market and complaints expressed by citizens since the policy was introduced even the government itself, is surprising and suggests that the impact of subsidy removal together with all other potentially inflationary reforms has had very insignificant effects on

inflation and questions the rationale for palliatives offered by governments and businesses in the first place. Most analysts have forecasted a hike in inflation of between 25-30% in June 2023 and the World Bank itself has postulated that an additional 5 million Nigerians have entered extreme poverty due to the policy.

Further review of the CPI data for June 2023 shows that the transport and the electricity, gas, and other fuels categories which we would expect to be substantially affected by the subsidy removal were not noticeably affected. Both these categories account for about 23% of the CPI. An analysis of the movement of these categories suggests a similar pattern of growth from January to June 2023 with June only exhibiting minor changes over May 2023, further suggesting very surprisingly, little of no impact of subsidy removal in the official data. A similar trend is observed in the month on month for food, transport and the electricity and other fuels categories.



Movement in month on month CPI across key categories Jan - June 2023

	All items	All items less Farm Produce	All items less Farm Produce and Energy	Imported Food	Food	Food & Non Alcoholic Beverage	Alcoholic Beverage, Tobacco & Kola	Clothing & Footwear	Housing Water, Electricity, Gas & Other Fuel	Household Equipment Maintenance	Health	Transport	Communication	Recreation & Culture	Education	Restaurants & Hotels	Miscellaneous Goods & Services
JAN/FEB	1.71	1.06	0.92	1.41	1.90	1.89	1.04	1.32	1.39	1.26	1.63	1.64	0.56	0.56	1.67	1.48	1.73
FEB/MAR	1.86	1.84	1.91	1.45	2.07	2.05	1.13	1.40	1.44	1.23	1.68	2.18	0.71	0.76	1.83	1.44	1.67
MAR/APR	1.91	1.46	1.44	1.46	2.13	2.11	1.13	1.43	1.46	1.26	1.71	2.23	0.73	0.80	1.88	1.67	1.72
APR/MAY	1.94	1.81	1.85	1.47	2.19	2.18	1.09	1.41	1.41	1.35	1.87	2.18	0.73	0.87	1.74	1.66	1.78
MAY/JUNE	2.13	2.74	1.77	1.74	2.40	2.38	1.24	1.57	1.61	1.38	1.95	2.41	0.83	1.09	1.83	1.80	1.88

	All items	All items less Farm Produce	All items less Farm Produce and Energy	Imported Food	Food	Food & Non Alcoholic Beverage	Alcoholic Beverage, Tobacco & Kola	Clothing & Footwear	Housing Water, Electricity, Gas & Other Fuel	Household Equipment Maintenance	Health	Transport	Communication	Recreation & Culture	Education	Restaurants & Hotels	Miscellaneous Goods & Services
JAN/FEB	22.91	18.84	18.37	18.52	24.35	24.24	17.23	17.36	18.11	17.19	19.07	21.43	10.54	14.13	19.53	17.84	19.63
FEB/MAR	22.04	19.86	19.63	18.58	24.45	24.32	16.72	17.25	18.19	17.07	19.50	22.25	10.30	13.48	20.08	18.04	20.01
MAR/APR	22.22	20.14	19.96	18.65	24.61	24.47	16.18	17.16	18.29	16.93	19.94	23.12	10.06	12.85	20.69	18.48	20.42
APR/MAY	22.41	20.06	19.83	18.72	24.62	24.68	15.56	17.03	18.31	16.86	20.51	23.87	9.77	12.25	21.07	18.90	20.87
MAY/JUNE	22.79	20.27	20.06	19.10	25.25	25.09	15.08	17.05	18.55	16.78	21.13	24.83	9.54	11.88	21.49	19.45	21.38

Impact of past and present PMS price adjustments on changes in inflation

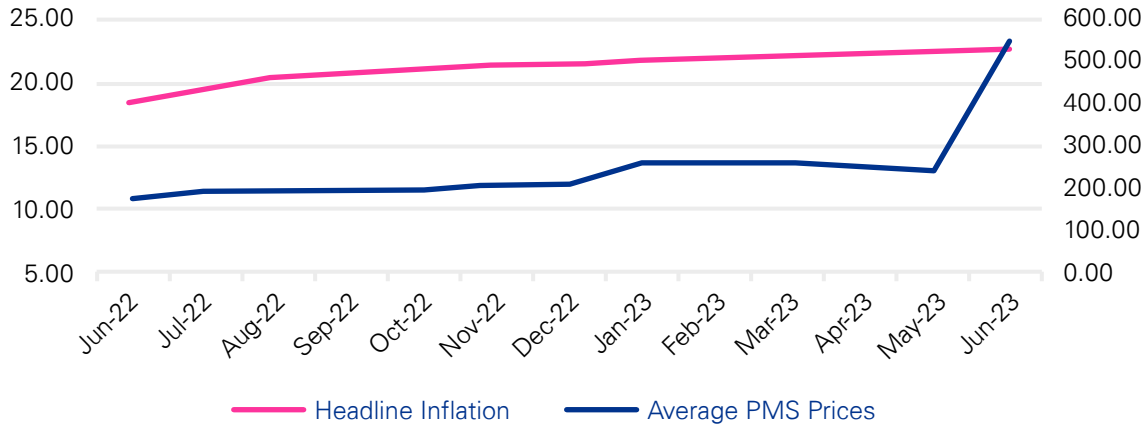
	MoM	YoY	PMS		
May - 23	1.94	22.41	Before	After	% Change
Jun - 23	2.13	22.79	185	545	196.20%
Growth (%)	9.79 %	1.70 %			
	MoM	YoY	PMS		
Apr - 16	1.60	13.72	Before	After	% Change
May - 16	2.80	15.58	87	184	111.49 %
Growth (%)	75.00 %	13.56 %			
	MoM	YoY	PMS		
Dec - 11	1.06	10.30	Before	After	% Change
Jan - 12	3.35	12.60	65	87	33.85 %
Growth (%)	216.04 %	22.33 %			

While yearly headline inflation represents another record inflation rate, the month on month change where a larger change would be expected between May and June is by no means the highest month on month inflation on record. While monthly inflation rose by 2.12% in June 2023 following subsidy removal it rose higher in December 2009 (2.2%), June 2010(2.91%), January 2012 (3.25%), February 2016 (2.3%), March 2016 (2.2%), May 2016 (2.8%).

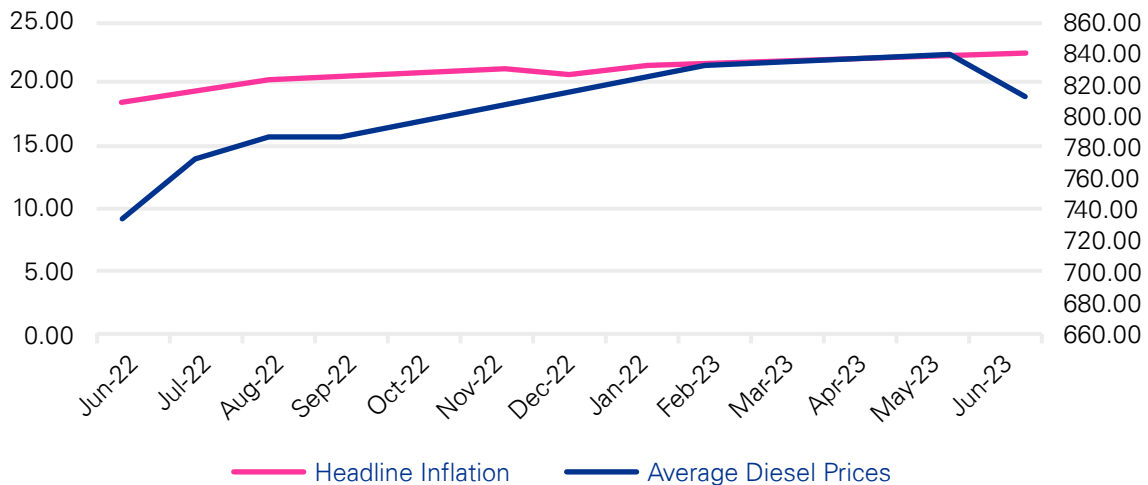
The official inflation data for June 2023 is even more surprising when you consider the other policy measures such as the adoption of the 7% VAT on imported diesel, the depreciation of the naira following the FX unification policy and the implementation of other aspects of the 2022 Fiscal Policy Act all introduced in the same month and all of which have the propensity to be inflationary. None of this is however showing in the June CPI data. One likely explanation might be a time lag between the policy and its inflationary impact, but this is unlikely as the effect of the

policy were immediate and very direct. Another possibility is the presence of another highly weighted component of the CPI that experienced a huge drop in price as to cancel out the increase from the PMS adjustments. However, every category increased but just marginally and largely in line with post PMS price adjustments. While Diesel prices have dropped from on average N844 in May 2023 to N815 in June, this cannot explain the almost 200% rise in PMS prices have little effect on inflation. The trend in PMS and diesel prices as well as trend in food inflation, transport inflation and energy, and other fuels inflation is therefore unexplainably out of sync with the trend in headline and month on month inflation in June 2023 as shown in the various charts below. While there is no clear explanation for the seemingly muted effect of the subsidy removal policy on inflation and there is no obvious explanations at this time to suggest a lag in policy effect, we will wait till the CPI is released for July 2023 to take a further review.

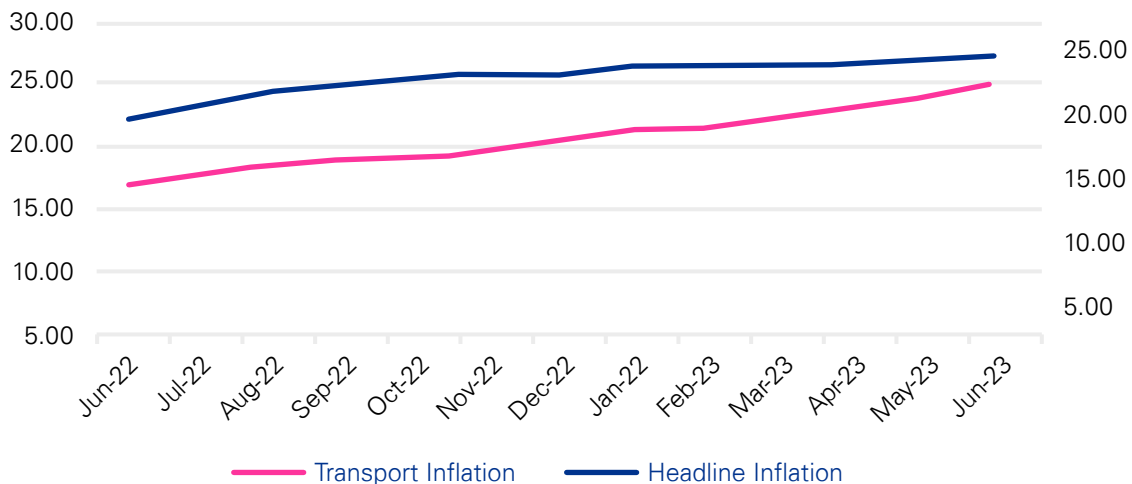
Headline Inflation Moving At A Consistent Rate Not In Sync with PMS Prices in June 2023



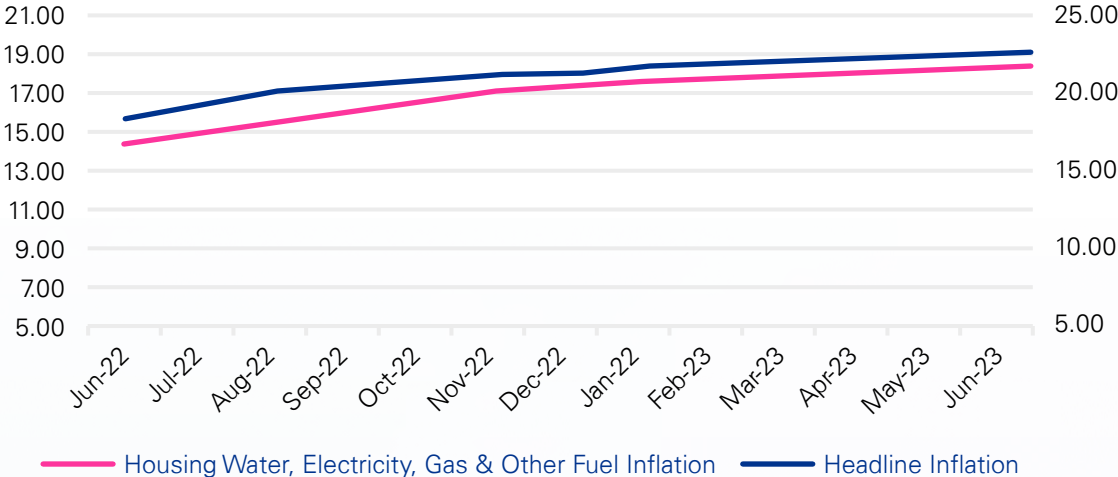
Headline Inflation Moving At A Consistent Rate Not In Sync with Diesel Prices



Transport Inflation and Headline Inflation Moving At Consistent Pace Despite SUSDy Removal in June 2023



Fuels Inflation and Headline Inflation Moving at Consistent Pace Despite Subsidy Removal in June 2023



For further information, contact:

Dr Yemi Kale

Partner/Chief Economist
KPMG Nigeria
Oyeyemi.Kale@ng.kpmg.com

Busayo Olanrewaju-Afuye

Associate, Research and Insights
KPMG Nigeria
Busayo.Olanrewaju-Afuye@ng.kpmg.com



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2023 KPMG Advisory Services, a partnership registered in Nigeria and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

