

Central Bank of Nigeria Communiqué No. 88 of the Monetary Policy Committee Meeting of Monday and Tuesday, March 18 and 19, 2013

The Monetary Policy Committee met on March 18 and 19, 2013 with all the 12 members in attendance. The Committee reviewed the conditions and challenges that confronted the domestic economy in the first quarter of 2013 against the backdrop of current international economic and financial developments with a view to reassessing the monetary policy options in the short-to-medium term.

International Economic Developments

At the outset, the Committee observed that global growth remained subdued throughout 2012 due to the softer than expected level of activities in the euro area and the slipping of Japan into recession during the second half of the year. Weak and fragmented growth was also recorded across major economies and regions including the US. The emerging market economies, however, showed a fair degree of resilience.

The growth outlook, however, appears promising. The IMF January 2013 WEO Update, projected a global output growth of 3.5 per cent in 2013 compared with the 3.2 per cent achieved in 2012. In the Advanced Economies, output was estimated at 1.4 per cent for 2013 compared with the 1.3 per cent achieved in 2012.

Recession is expected to continue in the euro area although the magnitude of the contraction, estimated at 0.2 per cent in 2013, represents an improvement over the 0.4 per cent contraction in 2012. A slowdown in growth is also expected in the US in 2013, as output is projected to decline by 2.0 per cent from 2.3 per cent in 2012, owing largely to the short term effects of its fiscal consolidation regime as well as the weaknesses in the labor and housing markets.

The emerging Asian economies were projected to post a gradual recovery that would propel global output growth in 2013. China, which previously recorded a slowdown over seven consecutive quarters to Q3 2012, witnessed improved activity in Q4 2012; confirming that an upswing in growth was underway. The recent fiscal and monetary easing operations of the Peoples Bank of

China led to increased tempo of investment in infrastructure with indications of further public spending in fiscal 2013. Thus, the economy is expected to grow strongly in 2013 amid gradual improvements in the external environment. Japan returned to growth in the fourth quarter of 2012, raising hopes of an end to the 15-year deflation. The major setback in the region is expected from India, with real GDP growth of 5.4 per cent in 2012 on account of the poor performance of the manufacturing, agriculture and service sectors.

The Committee noted that growth in Sub-Saharan Africa was still robust, although real output growth dropped to 4.8 per cent in 2012 from 5.3 per cent in 2011. The performance of Sub-Saharan Africa during 2013 would partly depend on developments in the euro area as well as the extent of recovery in China. With policy buffers weaker than they were prior to the 2008 crisis, the ability of governments to implement countercyclical fiscal policy may be constrained.

Domestic Economic and Financial Developments

Output

The Committee was satisfied with the relatively robust output growth projections for 2013 despite the slowing global economy, on the back of favorable conditions for increased agricultural production, the outcome of banking sector reforms, as well as other initiatives by government to stimulate the real economy. The National Bureau of Statistics (NBS) reported that the real GDP growth rate declined from 7.43 per cent in 2011 to 6.58 per cent in 2012. The decline was partly driven by the oil sector which contracted by 0.91 per cent. The major driver of overall growth, therefore, remained the non-oil sector, with agriculture; wholesale and retail trade; and services contributing 1.37, 2.19 and 2.10 percentage points, respectively.

The Committee was concerned that the declining contribution of the oil sector to growth, which became apparent in the second half of 2011, continued in Q4 2012. Crude oil production, including condensates and natural gas liquids, decreased by 37,000 barrels per day (bpd) in February 2013 to 2.054m bpd compared with the level of 2.072m bpd attained in December 2012. Oil theft in the Niger-Delta remained a source of concern. The Committee was

also concerned that the decline in the growth rate of agricultural output which started in the 4th quarter of 2011 continued up to the end of 2012.

The Committee was of the view that although the GDP growth projection remained high, there were a number of risk factors that were likely to affect output performance. These include perception of increased levels of corruption and impunity in the country, insecurity particularly in the northern part of the country, as well as mixed signals from power and petroleum sector reforms.

Prices

Headline inflation which had decreased to a four-year low of 9.0 per cent in January 2013 inched up to 9.5 per cent in February, driven largely by the food component. Food inflation, which was 10.1 per cent in January 2013, increased by 0.87 percentage point in February due mainly to increases in the prices of farm produce and imported food items. Core inflation, however, moderated slightly between January and February 2013. The Committee noted that the sharp drop in inflation in early 2013 compared with early 2012 is largely a result of the base effect of the partial

removal of fuel subsidy in January 2012. With the tapering off of the first and second round effects of the increase, the prudent monetary policy stance and stable exchange rates are yielding lower headline inflation figures.

Monetary, Credit and Financial Market Developments

Broad money supply (M2) grew by 2.86 per cent in February 2013 over the level at end-December 2012, which annualizes to 17.16 per cent. Aggregate domestic credit (net) grew by 10.17 per cent over the same period (an annualized rate of 61.02 per cent). The significant growth in net credit in the period was due to the huge increase in credit to government (net), which rose by 108.18 per cent.

Interest rates in the interbank money market declined between January 21 and March 14, 2013 owing to liquidity surfeit in the banking system. The interbank call and the OBB rates, which opened at 10.35 and 10.33 per cent on January 21, closed at 10.29 and 10.28 per cent, respectively, on March 15, 2013. The average interbank call and OBB rates for the period were 11.38 and 11.23 per cent, respectively. The average prime lending rate

inched up slightly from 16.54 per cent in December 2012 to 16.56 in February 2013, while the maximum lending rate more or less remained flat at 24.60 per cent during the period. The weighted average deposit rate, however, increased from 3.77 to 5.37 per cent during the review period.

The Committee noted the upswing in activities in the capital market, as equities market indicators all trended upwards in the review period. The All-Share Index (ASI) increased by 17.3 per cent from 28,078.81 on December 31, 2012 to 32,950.08 on March 15, 2013 while Market Capitalization (MC) rose by 17.5 per cent, from N8.97 trillion to N10.54 trillion. The Committee, however, observed that the improved performance was largely induced by the substantial portfolio inflows, as foreign investors took advantage of the favourable domestic environment brought about by the high yield on government debt instruments, and stability in the naira exchange rate.

External Sector Developments

At the Wholesale Dutch Auction System (wDAS), interbank and the BDC segments of the foreign exchange market, the exchange rate opened at N157.29/US\$, N157.10/US\$, and N159.00/US\$ on 22nd January 2013 and closed at N157.32/US\$, N158.65/US\$, and N160.00/US\$, respectively, on March 15, 2013. The average wDAS, interbank and BDC exchange rate during the period was N157.30/US\$, N157.65/US\$, and N158.94/US\$, respectively. The Committee noted the slight depreciation in the exchange rate at the wDAS and interbank segments of the foreign exchange market. The BDC segment, however, appreciated during the period due to the low patronage by speculators on account of the improved supply of foreign exchange by oil companies, increased inflow from portfolio investors, and the effect of the prohibition of the simultaneous access to the CBN window (Repo and Standing Lending Facility) and wDAS transactions by DMBs. The Committee expressed satisfaction with the significant accretion to external reserves which stood at US\$49.38 billion as at March 14, 2013, representing an increase of US\$ 5.5 billion or 12.68 per cent over the level of US\$43.83 billion at end-December 2012. The increase in reserves was driven largely by the proceeds from

crude oil and gas sales and crude oil-related taxes, as well as reduced funding of the wDAS. The reserves level could finance over 13 months of imports. The Committee urged the Bank to continue the monitoring of portfolio and foreign direct investment flows, while being conscious of the risks to financial stability of a rapid outflow of hot money.

The Committee's Considerations

The Committee was pleased with the prevailing macroeconomic stability despite shocks from both external and domestic environments; a development which informed the tightening stance of monetary policy since the third quarter of 2010. Having achieved a reasonable degree of moderation in the rate of inflation, there were compelling arguments to consider easing monetary policy, at least from the perspective of stimulating growth in the real sector. Given the slowdown in overall GDP and agricultural GDP growth, inability of the SMEs to borrow at the current lending rates, and crowding out effects may require monetary easing. The Committee carefully weighed the option of relaxing monetary policy against the likely risks in the near-to-

medium term, noting that reversing the current stance of monetary policy was not likely to produce a neutral outcome, as it may signal the preference for a higher inflation rate on the part of the CBN.

At 9.0 and 9.5 per cent in January and February, respectively, the price data, which largely reflected the base effect of the first and second round impact of the fuel subsidy removal in January 2012, sends a clear signal that there was still an upside risk to inflation in the near-to-medium term. Furthermore, yields on FGN bonds have been declining steadily, signalling the impact of increased inflows while equity prices have been trending upwards. Quantitative easing, especially in the US and the EU is already creating a potential new round of asset bubbles globally. The Committee was of the view that the growth in the domestic capital market was driven largely by the huge capital flows. The principal risk of stability in the medium-to-long-term can be addressed through diligent implementation of sound policies of fiscal consolidation and structural reforms. Without these, the economy will not be able to attract long term foreign capital inflow that makes the

gains of monetary policy sustainable and insulate the economy from the risks associated with external shocks and capital flow reversals. Monetary policy will, therefore, seek to preserve the current gains of macroeconomic stability.

The Committee also noted the wide spread between deposits and lending rates, which it attributed to the inefficiencies in the market requiring institutional and structural reforms that would enforce behavioural change on the market, consistent with the long term needs of the economy.

The Committee was of the view that sustainable low lending rates, could be achieved if the necessary infrastructure such as stable power and good roads, amongst others, were put in place. The Committee noted that the present infrastructural condition has always provided an incentive for asymmetric response on the part of the banks to the policy rate in a manner that was not always beneficial to the small and medium scale customers. With respect to the price level, the Committee observed that the rising pressure in February after a significant moderation in January, was

indicative of the fact that there were some underlying factors that could constitute a threat to inflation in the medium term.

The Committee noted the 2013 Federal Government Budget of N4.9 trillion, passed by the National Assembly and signed into law by the President, represents an increase of about 5 per cent. Furthermore, the budget, predicated on an oil benchmark price of US\$79/barrel as against US\$75/barrel, proposed by the Executive, potentially slows down the pace of fiscal consolidation with implications for accretion to the Excess Crude Account and gross external reserves. In addition, the Committee observed that the foreign exchange market has started experiencing pressure in March 2013, mainly reflecting compression of yields in the fixed income credit as well as outflows to pay dividends by multinational corporations. However, the Committee noted that the exchange rate has remained within the target range and also that the current monetary conditions are conducive to further tightening using Open Market Operations without recourse to an increase in the MPR.

In view of these developments, the Committee was faced with three choices:

(i) An increase in rates in response to the uptick in headline and food inflation; and pressure on exchange rates;

(ii) A reduction in rates in view of declining core inflation and GDP growth;

(iii) Retaining current monetary policy stance to sustain the gains of monetary policy while utilizing the existing space in the corridor to influence yields and exchange rates in the short term.

The Committee's Decisions

The Committee considered and rejected option 1 as being potentially unnecessary since there are no major inflationary concerns at this time. While acknowledging the merit of the arguments in favour of option 2, it was also rejected because it could send wrong signals of a premature termination of an appropriately tight monetary stance. The Committee, therefore, decided by a majority vote of 9:3 to accept option 3 and maintain the current policy stance i.e. to retain the MPR at 12 per cent with a corridor of +/- 200 basis points around the midpoint;

retain the Cash Reserve Requirement at 12 per cent and Liquidity Ratio at 30 per cent with the Net Open Position at 1 per cent.

Thank you.

Sanusi Lamido Sanusi, CON

Governor

Central Bank of Nigeria

19th March 2013

**PERSONAL STATEMENTS BY MONETARY POLICY COMMITTEE
MEMBERS**

1.0 ALADE, SARAH

Headline inflation decreased to 9.0 percent in January and edged up to 9.5 percent in February, 2013. This increase was driven mainly by increases in domestic food prices. In the international scene, the fiscal problems and budget cuts in the United States have the potential of dampening the pace of the global recovery. On the domestic front, the increase in the 2013 Budget benchmark oil price and the Government policy stance on the fuel subsidy regime remained possible pressure points and pose upside risks to inflation. Based on these, I am inclined to support a hold in Monetary Policy Rate (MPR) and Cash Reserve Requirement (CRR).

Global economic growth is still showing some signs of weakness.

Global growth is projected to increase gradually in 2013 as policy actions in the euro zone have lowered the risk of severe crisis. However, the cut-back in spending in the United States and the slide into recession in Japan pose risk to global growth prospects. In the euro area, although there is a return to recovery after a protracted contraction, low domestic demand and fiscal contraction in some European countries could delay economic recovery. In the emerging markets, coordinated policies have resulted in a modest growth pickup especially in China and Brazil, while growth in India remained weak. These mixed developments call for a cautious approach to monetary policy at this time, until conditions stabilize.

The single digit inflation should be viewed with cautious optimism.

Even with the achievement of single digit inflation in January and February 2013, tight monetary policy is still necessary to safeguard the economy as staff estimates suggest an upward trend in the coming months. The achievement of single digit inflation is a welcome development, signifying the benefit of past monetary policy actions and overall policy coordination that have helped

to sustain the improvement recorded in macroeconomic indicators. While there are strong arguments for monetary easing at this point, to aid credit creation and flows to the real sector of the economy among others, inflation edged up to 9.5 percent in February. In addition, monetary policy cannot be the sole cause of the lack of credit flow to the real sector. With risks such as depressed global growth and uncertainties in the domestic economy, a hasty monetary easing may not be in the interest of economic stability. It is well known that structural imbalances in the economy play a major role in the determination of high borrowing cost and without tackling these problems, there is a limit to what monetary policy can do. In addition, with the start of the raining season and commencement of the planting season, further upward pressures would be put on domestic food prices and overall headline inflation in the coming months, as consumable supplies dwindle.

Developments in the domestic money market suggest enough liquidity in the banking system. Money market rates have remained lower than the monetary policy rate and banks deposit in the Standing Deposit Facility with the Central Bank has been

very high. Similarly, average open buy back (OBB) and interbank call rates averaged 11.3 percent and 10.3 percent respectively since the last Monetary Policy Committee meeting in January, suggesting liquidity in the banking system. This development coupled with anticipated upward inflationary pressure would suggest that monetary easing at this time is premature.

The uncertainty surrounding oil prices could pose serious risk to the Budget. The 2013 Budget signed into law by the President was based on the oil price benchmark of US\$79.00 per barrel as recommended by the National Assembly in contrast to the US\$75.00 per barrel recommended by the Executive Arm of Government. The continued slow-down in global growth and increased domestic oil production in the United States have the tendency of lowering oil prices in the global market. This could have far reaching implications for the Nigeria economy in terms of decreased oil revenue; increased debt; and adverse consequences for external reserve build-up and volatility in the exchange rate. This would have a destabilizing effect on the economy and could undermine the policy gains of the past couple of years.

Base on the above, I recommend a hold on Monetary Policy Rate and Cash Reserve Requirement. In a situation of renewed inflationary pressure and weak global growth, there is a need for cautious approach to monetary policy and monetary easing at this time could be counterproductive.

2.0 BARAU, SULEIMAN

Background

Having deeply observed developments in the domestic and global economy since the last Monetary Policy Committee (MPC) meeting, I have come to the conclusion that no significant event has happened to make a change in the current stance of monetary policy. I have therefore, today, voted to maintain the status quo.

Developments/Discussion

Inflation – It is true that Headline Inflation trended down to single digit at 9.0% in January 2013. However, the fact that it went up to 9.54% in February does support my position that we need to observe consistent declining trend for all measures of inflation overtime for us to consider a change in our tightening stance. We

currently have mixed signals. While core Inflation trended down from 11.30% in January to 11.18% in February, Food Inflation increased from 10.10% in January to 10.97% in February. Imported Inflation also trended up to 14.33% in February from 14.10% in January. The direction is therefore not very clear. There is also the possibility of further inflationary pressure from liquidity injection due to the commencement of the implementation of the 2013 Budget. Upside risk to inflation may also come from higher electricity tariff, the effect of duty and higher tariff on rice import amongst others.

Exchange Rate: Exchange rates have been stable but we have recorded recent build-up of demand pressures, which led to mild depreciation across all market segments. The WDAS rate depreciated by 0.2% from N157.29/USD on January 21st to N157.32/USD on March 15, 2013. The Interbank and BDC segments of the market saw exchange rates also depreciating by 1% and 0.63% respectively as a result of demand and supply factors.

GDP Growth: Nigeria's GDP growth of 6.58% in 2012, though slightly lower than the level in 2011 was remarkably higher than global

GDP growth rate of 3.2% and Sub-Saharan African average of 4.8%. This strong growth level (though arguably below potential) was achieved in spite of the tight monetary policy regime in 2012. It is true that accommodative policy should generally help to elicit better growth performance, but what is required to unleash Nigeria's growth potential are the necessary real sector reforms and the removal of market distortions that should elicit better pricing of capital and other assets. In other words, access to cheap finance is necessary but not sufficient to elicit sustained growth. Structural reforms have to be implemented to gravitate towards growth enhancing sectors such as agriculture, manufacturing, among others.

Interest Rates: Market rates have been largely stable albeit taking a recent declining trend. The decline in my view is due to a combination of factors:

- Current liquidity in the system;
- Expectations of liquidity injection; and
- Expectation of reversal of tightening stance through the lowering of policy rates by MPC.

With inflation rate at 9.5% in February real interest rates have continued to be positive. But the decline in market rates has two significant implications for policy consideration:

- Yields on Government Bonds have trended downward with significant possible impact on profits;
- We are becoming less attractive to foreign investors seeking destinations that offer attractive return on investment. This has led to decline in foreign portfolio inflows and may impact negatively on further build-up of foreign reserves and the exchange rate stability. The MPC is aware of the very obvious risks associated with foreign portfolio inflows and many would argue that being a less attractive destination for such flows is a positive development. I am happy to note, however, that while MPC does not target portfolio inflows, their positive impact on the build-up of foreign reserves, stability of the exchange rate and creation of liquidity in the capital market have been noted. The risks associated with such inflows in the management of foreign reserves and exchange rates are very well noted and appropriate measures would be taken in due course to mitigate them. What is also required is the complementary measures in the capital market to remove the possibility of asset price bubble as well as possibly ensuring that exits are well controlled and managed.

Foreign Reserves: At US \$49.3billion, the foreign reserves position is at a healthy level and is sufficient to accommodate 13 months of import. The healthy growth has been on the back of good oil prices and significant portfolio inflows. The healthy foreign reserves position has supported the stability of exchange rates.

Riding on the back of increased market liquidity and portfolio inflows, we have recently witnessed increased demand pressure at all foreign exchange market segments. The maintenance of the current tightening stance would help to ensure the continued stability of the exchange rate and sustained build-up of foreign reserves.

Market Expectation/Sentiment: Recent commentaries in the media understandably favoured reduction in MPR and the possible adoption of accommodative (effectively a reversal of current tight stance) monetary policy stance. This view is perhaps predicated, as I understand it, on the following points;

- MPC has maintained the existing stance of policy for over a year;
- It is probably somehow boring;
- The decline in inflation rate in January, buildup of foreign reserves and stability of exchange rates at this point in time; and
- The high lending rates and their adverse impact on economic growth.

I have the following response to these issues, not in any particular order:

- MPC decisions are not based on emotions or sentiments. MPC members are presented with current numbers and facts on local and global developments. Members factor in pressure points and review outlook in order to take well guided decisions. After a careful review of where we are and the outlook, it is my judgment that we should maintain the status quo.
- MPC decision is about rational choice. It is about price and monetary stability. We had, in my judgment, focused on inflation and exchange rate with modestly profound outcomes. Lending rates are unacceptably high because of the unusually high cost of doing business in Nigeria which current efforts at structural reforms would help to reduce. Fixing the structural issues would have a salutary effect on our growth trajectory. It will also help to deliver more acceptable lending rates. The MPC and the Central Bank of Nigeria would continue to promote price and monetary stability conducive to growth. The limitation of monetary policy must, however, be recognized by the market.

Conclusion: It is in the light of the foregoing that I voted as follows:

Maintain MPR at 12% with the corridor of +/- 200 basis points

Maintain Cash Reserve Ratio (CRR) at 12%

Maintain Net Open Position (NOP) limit at 1%.

3.0 GARBA, ABDUL-GANIYU

I vote to:

1. Reduce the MPR by 0.50% to 11.50%.
2. Maintain the asymmetric corridors at $\pm 2.0\%$ around the MPR.
3. Maintain CRR at 12%.

The Context of Decision

1. The tightening regime and the complementary institutional changes that the MPC implemented from September 2010 have been successful in maintaining price stability, exchange rate stability and narrowing the exchange rate premium.

2. As with all macroeconomic policies and indeed, all economic choices, the laws of trade off and opportunity costs have prevailed. The sacrifices in terms of forgone real GDP growth and, rise in unemployment have been significant. The tightening would have been far more successful at much lower costs had fiscal policy been more efficient and effective in enhancing the competitiveness of the Nigerian economy through upgrades in infrastructures and delivery of sound public services.

3. In an increasingly interdependent world, laws of trade off and opportunity costs are also at work constraining the effectiveness of policies in smaller open economies. For while the MPC's has had to tighten monetary policy to achieve stable price and exchange rates, major global players (the US FED, the Bank of Japan, The

European Bank and the Bank of England) have been using aggressive quantitative easing to reduce rates and weaken their currencies to stimulate their economies and enhance their competitiveness. The immediate consequences for Nigeria are the above trend inflow of portfolio flows into treasury bills, bonds and more recently, the capital market and, a crowding-out of FDI flows into the real sector.

4. The volume of portfolio flows into the Nigerian capital after the US FED's QE3 in September 2012 have stimulated growth in asset prices reminiscent of 2007-2008. Prior to QE3, portfolio flows have poured into government securities. These flows have expectedly, not promoted budget discipline, efficient allocation of credit, economic growth or job creation.

5. Although, some Central Banks play down global tail risks, it would be unwise for the MPC and Nigerian fiscal authorities to do so. The ongoing bail-out crisis in Cyprus and the response of global stock markets to the crisis is a reminder of how fragile and volatile the global financial markets are. The simultaneous co-existence of

record stock market indexes and record sovereign debts, high unemployment and slow growth point to a fragile global economy. The risks of currency wars, asset price bubbles, exportation of inflation and new rounds of macroeconomic and financial crisis call for (1) a forward looking policy stance, (2) continuous monitoring of the global economy also, the behaviors of strategic players –private and government; monetary and fiscal and (3) creative reaction functions.

The Basis for Decision

6. I decided in favor of a cut in MPR by 25 basis points in January to signal “a commitment to macroeconomic stability now and, in the future and, to avoid history repeating itself at an even greater cost.” Nothing has happened between January and now to convince me that I made the wrong decision. On the contrary, the underlying asset price bubbles in the major capital markets globally and, its “contagion effects” on the Nigerian capital market convinces me that the observed flows and market movements are not sustainable in Nigeria and globally.

7. Even more pressing now, is the need to begin the process of stimulating the economy in the light of the well-established evidence of consistent slowing down since the third quarter of 2010 and, of a consistent growth in unemployment. While it is true that underlying fiscal, institutional and structural problems are key constraints to growth, it is also true that interest rates correlate negatively with growth. What is needed therefore, from monetary perspective is to strengthen the potential effects of lower MPR rates on growth by creatively deploying existing options and institutions to directly address the malfunctions in financial markets. The key is to work through incentive system embedded in institutions to improve the operational and allocative efficiencies of Nigerian players and, of the Nigerian financial markets in which they “game with” global players: their loss is Nigeria’s and vice versa.

8. Reducing MPR by 50 basis points also signals to the fiscal authorities a commitment to price stability conducive to growth as well as a demand from them, of a commitment to fiscal discipline conducive to job creating growth with price stability. The two

commitments are necessary to sustaining growth, to reducing unemployment and to building the capacities that Nigeria will need to mitigate the potentially damaging effects of the ever frequent episodes of global tail risks crystallizing.

4.0 LEMO, TUNDE

Relative to the entire FY 2012, both headline and core inflation witnessed considerable moderation in the first two months of FY2013 with headline in particular falling into single digit, justifying the current tight stance of monetary policy. On the basis of the seemingly evolving benign macroeconomic environment therefore, arguments could be advanced for relaxing the current stance of monetary policy with the intent of stimulating real output growth.

I have a couple of concerns, however, with loosening of monetary policy so soon. There was a significant moderation in headline inflation in January due, among others, to base effect while in February, there was a renewed upward pressure on the price level coming mainly from farm produce as a result of transport cost.

Developments in these two months, therefore show a conflicting signal about the near to medium term path of inflation. Furthermore, staff forecast, based on the prevailing stance of policy, showed that inflation would be in the upper part of single digit for a reasonable portion of FY2013. As a result, loosening of monetary policy implies that the monetary authority is willing to accommodate double digit inflation level.

Besides, the Federal Government Budget for FY2013 with estimated total expenditure of about N4.9 trillion could be adjudged less expansionary in view of the moderation in the fiscal deficit/ GDP ratio. However, when consideration is given to the higher benchmark of US\$79/barrel of crude oil in the face of downward swings in the international price of crude oil, it is not unlikely that the actual fiscal deficit would exceed the budgeted level with implication of crowding out the private sector as well as further pressure on domestic interest rate.

Furthermore, oil production has been facing some challenges since the second half of 2012 with actual output falling below the

target. When this development is added to the adoption of a higher benchmark price of crude oil in the budget, it implies that the capacity to build up the excess crude account is reduced and thereby intensifies the vulnerability of the economy in the event of adverse shock to oil price. The current level of external reserve, which is gradually closing up with the pre global financial crisis era, has been the result of both demand and supply factors.

On the supply side, stable exchange rate coupled with high interest rate in the face of declining yield in other climes have significantly enhanced inflows of foreign capital while the increase in the Cash Reserve Ratio and Net Open Position of banks have worked on the demand side. There appears to be slight change in the tide on the foreign exchange market as it came under demand pressure in the month of March with the naira recording a marginal depreciation.

While it may be argued that a loosening monetary policy stance with the attendant reduction in lending rate would have a salutary effect on the harsh production environment, my view is

that the current production challenge goes beyond the confinement of rising cost of funds. It requires broad based reforms in critical infrastructure such as power and roads, including addressing the current security challenge with a view to improving the competitiveness of the business environment.

In the light of the absence of a clearly discernible lower path of a future price level coupled with the risks identified above, I propose that the current tightening stance of monetary policy be maintained by holding both the MPR and the CRR at the current rates.

5.0 MOGHALU, KINGSLEY CHIEDU

I vote to maintain the status quo and keep the Monetary Policy Rate at 12 per cent (plus or minus 200 basis points), the Cash Reserve ratio at 12 per cent, Liquidity Ratio at 30 per cent, and the net Open Position of banks at 1 per cent.

Despite strong arguments to reduce the MPR on the grounds of presumed pro-growth stimulus, concerns about the impact of an MPR of 12 per cent on the availability of credit to the real sector, and fears about the long-term implications for stability of an MPR regime that encourages inflows of speculative capital (hot money) – concerns that I fully share, I vote the position I have for the following reasons.

First, we remain at this time faced with a tension between foreign exchange stability and the need for long-term structural stability. The exchange rate looms large, and its stability remains critical, because Nigeria remains an import-dependent economy. Unless and until this fundamental changes for the better – which requires structural reforms in the larger economy to provide better infrastructure and ensure that Nigeria's petroleum refineries function at full capacity among other measures – maintaining exchange rate stability in the short term will remain critical as one instrument to control inflation.

The expectations in some quarters that the MPC should reduce rates does not give adequate recognition of the responsibility of structural economic policy – which in the long term is a fiscally driven process – in creating the inevitability of the monetary tightening stance the MPC has pursued for the past two years. Thus the CBN has become a convenient target for the venting of frustrations that should be directed at the adequacy of wider structural economic policy beyond monetary policy. Were the MPC to fail in its core responsibility of maintaining price stability – while being mindful of growth – chaos would result from a situation in which inflation could gallop out of control. As it is, however, an independent MPC needs to be far more mindful of inflation expectations than pressures to take steps based on populist or analysts' sentiment.

Second, and most important, it is clear from the data on prices that, while inflation fell into single digits in January 2013, data for January – February 2013 do not yet constitute a trend of falling inflation strong enough to reduce rates at this time. While staff inflation estimates point to a downward trend in the months

ahead, the consistency of the actual trend in the next two to three months with projections would form a stronger basis for loosening the monetary stance. In a mixed signal, respondents to a market intelligence survey expect elevated inflation rates in the short to medium term.

Moreover, even the sustainability of possibly lower rates in the near future is debatable if we factor in the impending elections season starting from 2014. What this situation points to is the inevitability of structural reforms in the economy and reducing the economy's absolute dependence on oil revenues over the next two to three years, while monetary policy holds the fort of stability until such a time as infrastructure upgrades begin to ginger output production. Effective power sector reforms, other infrastructure, and an increased effectiveness and diversification of revenue generation are the conditions that will spur weakening economic growth.

Third, the 2013 budget is still an expansionary one, and with the benchmark price at \$79, above the \$75 recommended by the executive arm of government, the implications for fiscal

consolidation and accretion to the Excess Crude Account and overall reserves are not positive. Combined with the sharp increase of credit to government by 108.18 per cent, inflationary threats have not dissipated. Reducing rates at this time will therefore send the wrong signal by encouraging inflation expectations. A recent staff study has found that the inflexion point at which inflation begins to hurt economic growth in the Nigerian economy is between 10.5 and 12 per cent.

There is not a great deal of difference between that range and where we are at this time – headline inflation increased year-on-year in February 2013 from 9 per cent to 9.54 per cent, and month-on-month from 0.62 per cent to 0.75 per cent. If we accept that core inflation is believed to be a better gauge of the impact of supply and demand on GDP than headline inflation because the former excludes food and fuel prices which tend to be volatile while the latter encompasses all the factors of inflation, it is cold comfort that core inflation was at 11.18 per cent in February compared to 11.30 per cent year-on-year and declined from 1.40

per cent to 0.00 per cent month-on-month. It appears that this was a base effect.

Given the overall structural problems confronting the Nigerian economy, there is little likelihood that a marginal reduction of the MPR will lead to a reduction in the interest rates charged by banks to borrowers. If this outcome cannot be guaranteed, why take the risk of reducing rates at this time and lowering our guard against inflation?

The work of the MPC is important, and the committee must continue to discharge its responsibilities. But, unless and until structural economic reforms kick in over the next few years, monetary policy must remain, at best a guardian of the flame and at the worst, a necessarily short-term medicine for symptoms in the hope that a long-term cure will be administered by overall economic policy to address fundamental causes.

6.0 KIFASI, D. I.

The 2013 Budget was designed against the backdrop of global economic uncertainty. Growth in the US is forecast to average only 2 per cent in 2013. Similarly, the near-term outlook for the Euro area has been revised downwards, with growth expected to contract by 0.2 per cent. In Asia, the short-term outlook for Japan is weak, with the Japanese economy expected to expand by only 1.2 per cent in 2013. Overall, global growth will average 3.5 per cent in 2013, a moderate increase from 3.2 per cent in 2012.

In spite of the turbulent global economic environment, the Nigerian economy has been resilient, experiencing a robust growth of 6.58 per cent in 2012 compared with global growth of 3.2 per cent. Inflation is now down to single-digit at 9.5 percent in February 2013, compared with 11.9 percent in February 2012. Our fiscal deficit is on a downward trajectory, and below our threshold of 3 per cent, while the exchange rate has remained stable.

Government remains focused on critical economic and social sectors. Some of these sectors are largely driven by private sector

activity, while others require a great deal of public sector support. The Government recognizes that our manufacturing sector cannot grow without a reliable source of long-term finance and more affordable interest rates. Approval has been given to restructure existing Development Finance Institutions (DFIs) as retail outlets for financing domestic lenders, while we build a strong wholesale institution that will increase lending and drive lending costs down.

In view of the above and given the current level of inflation (9.5% in February, 2013) and its projection to fluctuate between 8.8 per cent and 10.0 per cent in the next six months, I recommend that the MPR be moderately reduced by 50 basis points from 12% to 11.5% in order to stimulate real sector production while the current policy on foreign exchange be sustained to consolidate the relative stability achieved thus far.

7.0 OLOFIN, SAM

The economy is far from being on a stable equilibrium path; therefore it would be wrong to suggest that an auto-pilot

monetary policy stance is what we need, in a global economic environment that is still fraught with uncertainties, particularly in the Euro zone and the U.S that are the country's major trading partners.

The truth remains however that over the last several quarters, there have been no significant changes in the economy's fundamentals to warrant a major shift in monetary policy stance. Our strategy has been that of ensuring stability in the short to medium term, as efforts continue on the fiscal front, to bring about necessary structural transformation of the economy. This is critical if we are to grow the real sector of the economy and reduce its vulnerability to any likely price shock that may significantly affect export earnings and government revenue.

One of the major policy issues we are confronted with at this meeting like in previous recent meetings is on when and how, we would need to send appropriate signal(s) on major policy shift. In other words indicating that time is ripe for the Committee to embark on an accommodating monetary policy stance that

would be deliberately pro-growth. This of course would also require that we consolidate the gains from the tight monetary policy stance that has been in place ever since the MPR was jerked up to 12 percent along with other ancillary tight monetary policy measures.

Staff reports indicate that in the short to medium term developments in the global economy may among other things portend the following for the level and direction of domestic economic activity. First, a slow-down in global output particularly in the Euro area may be capable of reducing demand for oil, with negative implications for government oil revenue and overall level of economic activity. Decline in oil revenue would impair budget implementation and possibly increase the size of fiscal deficit. A fall in oil price would not only reduce government revenue, in the absence of compensating private sector flows, it would also reduce the rate of accretion to reserves and exert pressure on the exchange rate.

On the domestic front, over-all GDP growth though slowing remains robust at a projected rate of 6.75 percent for 2013. Headline inflation which for the first time in recent times climbed down to a one-digit level of 9 percent at the beginning of Q1, 2013, inched up again slightly to 9.5 percent in February, 2013. Similarly month-on-month food inflation rate rose slightly from 10.10 percent to 10.97 percent over the same period and imported inflation also rose from 14.10 in January to 14.33 in February 2013. However core inflation declined slightly from 11.30 percent to 11.18 percent.

On the fiscal side the passing and signing of the N4.9 trillion 2013 budget represents an increase of 6.2 percent over the 2012 budget and may be adjudged expansionary, with potentials for exerting inflationary pressure. Appreciation of equities in the capital market has had more to do with portfolio inflows than to changes in economic fundamentals.

Given the foregoing, one may conclude that the major monetary policy challenges in the short to medium term among others

include the following: managing inflation and exchange rate expectations to ensure price and exchange rate stability; sustaining the current rate of accretion to foreign reserves which as at March 14, 2013 stood at the level of \$ 49.38 billion; sustaining positive real interest rate, to increase our competitiveness in attracting net inflows, potential long term destabilizing effects of reverse hot money flows notwithstanding; and reducing the lending rate, and the still widening gap between lending and deposit rates.

All said and done, there appears to be still strong evidence on the need to tread the path of caution, by maintain the status-quo, until we have sufficient evidence to show among other things, that the observed decline in erstwhile double-digit inflation rate in Q1, 2013 is an indicator of a downward trend; secondly that the threat of a possible oil price shock is abating, as the pace of global economic recovery gathers strength; and finally as we have more evidence that the ongoing fiscal reform agenda is beginning to yield desired results of gradual structural transformation of the economy. Consequently, barring any major

significant in-between meetings domestic and or/or external developments that may warrant major policy review, I vote for the retention of all the elements our current policy stance.

8.0 OSHILAJA, JOHN

I voted today to maintain the current Policy stance, with all applicable parameters unchanged because available information, in my opinion, did not warrant any changes. In fact I perceived risks of slippage, in gains thus far achieved through policy actions, if markets misread signals of the Committee's resolve.

Followers of recent public speculation about the direction of Monetary Policy might be forgiven for wondering if local policy analysts appreciate the debilitating effects of market volatility. The fact is, unless markets are broad, liquid and orderly, volatile financial prices are inimical to sustainable economic growth. What the MPC's mandate directs us to promote is monetary stability. Specifically, price stability. To this end, the MPC expends considerable effort and diligence in promoting monetary

conditions needed to achieve price stability on a sustainable basis.

With lower inflation, the popular argument goes, the Central Bank's Policy Rate should be reduced, so that credit can be extended on more affordable terms. Affordable credit will lead to increased business activity, which in turn would call for increased employment and economic expansion. Really? I don't think so. Not because the argument is wrong, but because the Nigerian economy is still struggling to achieve the assumed preconditions on which this argument stands.

The Nigerian economy has experienced eras of cheap credit before. Largely owing to weakly governed institutions, profound inconsistencies in the structure of the economy, and substantial deficits in basic 20th century infrastructure, outcomes of loose credit policies have been overwhelmingly disappointing, and exceedingly costly. Economic planning has only lately started coming to terms with key strategies and resources needed to drive development meaningfully forward. But the required

structural reforms are still in vulnerable, early stages of progress. In the absence of tangible structural changes, most of which demand fiscal and not monetary measures, it would be intellectually dishonest for the MPC to recreate unsustainable monetary conditions of the past, and represent these to the Public as positive indications of future potential. It goes without saying that unsustainable monetary conditions are not what we are committed to.

So far, since 2009, the MPC has managed to restore essential Policy Transmission functions of the banking system, stabilize the exchange rate, attract foreign portfolio investment and establish real rates of return for domestic savers. All the while, the economy demonstrated comparatively firm rates of real but essentially low-quality (i.e. jobless) growth; buoyed by high oil prices, and fiscal and monetary interventions. Protracted sluggishness, in the economies of major trading and development partners, is now softening Nigeria's rate of economic expansion. Hence it's understandable that calls for monetary accommodation become more vocal. However, papering over structural economic

problems with cheaper domestic credit, is not an advisable growth strategy. Nigeria has been there, done that (on several occasions) and it never led to sustainable development solutions. As I see it, the economy does not yet have enough of a base of productivity-enhancing factors needed, to decisively keep inflation low enough for credit expansions to underwrite meaningful high-quality growth.

Measures of inflation taken over the last two months appear to be heading in the desired direction, i.e. downwards. CBN Staff forecasts for the next 6 months see Headline inflation fluctuating in a range of between 8.8 and 10 percent, with Core inflation expected to track a tighter 8.1 to 9.10 percent range. Further available data points suggest the makings of a disinflationary trend, but do not as yet confirm this trend. Until these forecasts begin to actually play out as desired, changing the current restrictive stance of Monetary Policy, in my view, risks incorrectly signaling a willingness by the Central Bank to forgo exchange rate stability in favor of foreign currency reserve accumulation. Not only would this be erroneous signaling, it would be a totally

unnecessary trade-off to make at this time. There are more effective tools, readily available to the CBN, for addressing excessive, short term, rate and currency market fluctuations. For example: Open Market Operations (OMO), by which central banks conventionally withdraw and inject banking system liquidity.

Signaling a change in Policy stance when currency exchange pressures are evident also opens another world of trouble for an economy that's globally competing to maintain Investor Confidence. Dawdlers on pending investment legislature might wish to note that Foreign Portfolio Investment in Nigeria (FPI) has consistently outstripped Foreign Direct Investment (FDI) by wide margins each year since 2009. FPI was roughly six times the level of in-bound FDI recorded by the CBN in 2012. This is purely financial, and not real, capital. Meaning that it is easily transferable, which makes it inherently unstable and therefore not an ideal form of capital to use to rebuild financial buffers. Looked at in another way, FPI is "rented" capital, and one of the implicit terms of this "lease" to the nation is a reasonably predictable rate of change in currency values. The point being that in frontier

financial markets like Nigeria's, excessive currency volatility remains a deal-breaker.

Another, more fundamental, reason for continuing Monetary caution at this stage lies with the current posture of Federal and State Budgets. Notwithstanding creditworthy Federal efforts made to rationalize its recurrent expenditures, and step up public investments while rebuilding fiscal space, theirs is still an expansionary budget. In fact, overall Nigerian Fiscal policies may end up becoming looser than advertised, with recourse to comparably low savings and/or borrowing, if either oil export production falls short of targets, oil market prices unexpectedly collapse – or both. Hence, the pace and quality of Budget executions has to provide further reassuring markers to enable the Committee to determine whether Monetary Policy needs to remain countercyclical or adopt pro-cyclical positions.

The MPC tends to be forward-looking and anticipatory when forming most judgments. At this stage in the rate cycle, however, I would like to see a well-established down-trend in inflation, more

consistent, complementary market operations by the CBN and, in the absence of negative external shocks, further encouraging signs of Fiscal performance, particularly on non-inflationary features of the nation's budgets. With these in play, I believe the Committee would have credible reasons for reassessing the current Policy stance.

9.0 SALAMI, ADEDOYIN

At 9.5 percent, the rate of increase in the Composite or Headline Index in February, compared with prices a year ago, is slightly higher than the 9 percent recorded when prices in January were similarly, placed side-by-side prices 12 months earlier. Food prices were 11percent higher in February while core inflation rose 11.2 percent. In contrast, January figures reported for both components of inflation were 10.1 percent and 11.3percent respectively. The detail provided for these figures show both imported and local food prices rising whilst non-food prices remain 'sticky'.

In my comments after our meeting in January, I concluded that “I would like to see a sustained trend of easing inflation numbers to be convinced that monetary policy should ease”. While the snapshot of price conditions in February 2013 provides another sub 10percent data point, it does not establish a trend. Furthermore, Staff forecasts of inflation in the next 6months suggest continuing volatility driven by a combination of ‘base’ effects and seasonality. Indeed, Staff forecast that the rate of change in headline prices between March and August 2013 will average 9.6 percent and range between 8.8 – 10 percent – with the trough being in March. Similarly, while the low point for Food price increase is expected to be 9.2 percent in March, average rate of increase in the next six months is estimated at approximately 11 percent with a peak of 12.1 percent in August. Over the same period, the average rate of increase in Core Inflation is projected to be 8.2 percent with a low point at 7 percent.

Beyond the absence of a discernible direction for inflation, there are other concerns which make a ‘hold’ decision, in my judgment, the right decision at this time. Presidential assent to the

2013 Appropriation Act, which has adopted US\$79/barrel as the benchmark price of oil, creates a fiscal environment which is looser than is warranted at this time, especially as the count-down to the 2015 General Elections has commenced. Total spending by the Federal Government of Nigeria, including the Subsidy Reinvestment and Empowerment Programme (SURE-P), in 2013 amounts to NGN5.26trn. This level of spending represents a 12 percent increase in relation to the 2012 budget. Compared to the provisional data for actual spending in 2012, the spending provision in the 2013 Appropriation Act is 27.3percent higher. In other words, fiscal policy is expansionary. That the signing of the Appropriation Act was immediately followed by an announcement that a supplementary budget would be forwarded to the National Assembly to correct areas of disagreement between the executive and Legislative Arms of government, creates further uncertainty about the stance of fiscal policy. We would have to wait until enactment of the Supplementary Bill to properly determine the stance of fiscal policy.

A popular refrain ahead of this meeting in support of an easing of monetary policy is the misalignment of interest rates. With the Monetary Policy Rate (MPR) higher than market yields and the Central Bank's Standing Deposit Fund (SDF) paying better than OMO, the MPR, the argument suggested, had to be eased into alignment with market rates. The hope of proponents of this view is that the anchor policy rate would fall to ensure alignment. This view then extends to suggest that bringing the MPR in line with markets rates would translate into lower borrowing costs. In my view, easing market rates are indicative of 2 things: (i) easier monetary conditions; and (ii) over-adjustment of market rates. That easing market rates point to easier monetary conditions is supported by the increase in average Banking industry liquidity from 68percent in December 2012 to 70.7percent at the end of February 2013. I would thus expect that market rates will soon correct themselves to reflect the stance of Monetary Policy.

A subtext of the argument for reducing the Monetary Policy Rate (MPR) concerns the impact of monetary policy decisions on the cost of credit. In on-going work exploring the relationship between

the MPR and key macro- economic parameters between Jan 2007 and Feb 2013, VAR analysis suggests that while there is a positive and significant relationship between the MPR and the Maximum Lending Rate (MLR), the relationship between MPR and the Prime Lending Rate (PLR) is insignificant. Though the insignificance of the relationship between MPR and PLR is surprising, it is consistent with the observed concentration of access to credit – the top 100 borrowers account for approximately 40percent of total lending.

These preliminary results seem to confirm that whilst the prime borrowers exercise market power in their borrowing relationship with financial institutions, the lenders dominate other borrowers. An important question which then arises is how much of total economic activity comes from the top 100 borrowers, who account for 40percent of lending? Providing answers to questions of this nature will enable determination of the growth impact of monetary policy decisions.

Recent pressure on the Naira serves as a warning of the currency challenges with which monetary policy may have to deal. With Portfolio Investment inflow of \$13.413bn in 2012 and an average of US\$2.13bn in the first two months of 2013 – 85percent of which went into the Equity Market, the challenge of managing capital outflows as international investors change portfolio allocation decisions cannot be understated and should therefore not be underestimated. While it is clear that foreign savings cannot be expected to be more than supplements for domestic savings, the exchange rate stability which portfolio inflows have enabled affords time, though limited, to meaningfully embark on the process of structural reforms which reduce our exposure and vulnerability to external events.

10.0 UCHE, U. CHIBUIKE

At the last MPC meeting in January 2013, I was part of the minority that voted for a cautious reduction in MPR which had for over one year remained at 12 percent. Developments in the past two months have further strengthened my belief in the need for MPC

to rethink its position and signal an end to its current tight monetary policy stance in a cautious and responsible way.

I am particularly emboldened by the fact that our base rate remains in positive territory as inflationary pressures continue to moderate albeit mildly. The inflation trend analysis for 38 months suggests that inflation volatility has reduced and that headline and core inflation are on the decline. It is important to note that both the headline and core inflation which currently stand at 9.54 percent and 11.18 percent respectively (February 2013) are both below the current MPR.

The consequences of the high MPR and tight monetary policy stance of MPC remain obvious. It has for instance provided little incentive for the development of the real sector which is central to the attainment of sustainable economic development in our country. This has been complicated by the increasing margins between the lending and borrowing rates in our economy. It is public knowledge that the excessive interest rates banks charge

on loans and advances is a major impediment to economic development and even the health of our financial system.

Furthermore, despite the high MPR, deposits in the banking sector continue to earn negative real returns. On the other hand, banks charge borrowers' rates that double or even triple the MPR rates. The consequence of the above is that the high MPR is basically being exploited by the banks. Depositors are simply being forced to subsidize bank profits in an oligopolistic market. In the long run of course both banks and depositors will lose. This is because there is always a positive correlation between the health of banks and that of the underlying economy. Any monetary policy model that does not recognize this fact cannot, in my view, be sustainable. As I made explicit in my last MPC policy statement:

The belief that banks in a rentier state where information inefficiency thrives will through moral suasion behave in a less predatory manner with respect to interest rate policies is erroneous. The current data which shows that banks are gradually returning to their mega profit declaration days sometimes with

little respect for existing CBN rules is clear evidence of this. We therefore need to do more to curtail the widening gap between banks' deposit and lending rates.

At another level, as in previous MPC meetings, I have always disagreed with the “popular view” that maintaining high MPR makes Nigeria competitive with respect to attracting Foreign Direct Investments. This is because most of these so called FDIs are simply speculative capital looking for short term profit outlets. This kind of capital does not develop economies. Admittedly, attracting such monies usually help central banks to curtail exchange rate pressures. This however happens only in the short run. History has shown that speculative capital is always volatile and economically destructive in the long run. The reverse flow of such capital can easily put pressure on both currency exchange rates and the capital market. The recent pressure on the Naira is no doubt, at least in part, a consequence of FDI flow reversals. Few will also dispute the fact that speculative FDI is partly responsible for the current appreciation of share prices in Nigeria. Such influences are clearly not sustainable.

For the avoidance of doubt, I have always conceded the fact that the tight monetary policy stance of MPC has helped curtail inflation in a rent economy with a long history of government fiscal indiscipline. Despite this, it is important to carefully weigh the costs of the tight monetary policy stance against its benefits. In undertaking this balancing act, I am of the view that, even with MPC's best efforts at maintaining price stability, the relatively high global oil prices have been the most important ingredient in the attainment of monetary policy stability in Nigeria in recent times. Any material adverse change in international oil prices will spell doom for our exchange rates, reserve accretion, inflation and even political stability.

In the light of the above therefore, it is important that MPC should always maintain objectivity in measuring its monetary policy stability achievements. The real challenge for MPC is to develop and promote policies that will grow the real sector in order to diversify the economy away from oil rents. Doing this, especially given the peculiar fiscal policy management complications of our

country, will not be easy. Any little progress we can make in this direction will by far outweigh the short term benefits (which the MPC even with its best efforts cannot guarantee) of crowding out the real sector with high MPR in the guise of promoting monetary stability. Whatever we do, it is always important to keep in mind that monetary stability cannot be an end in itself. It makes sense only when it helps promote real sector growth and development. The argument that reducing MPR will not translate to any material increase in credit to the real sector should not stop MPC from moving in the only direction that can help in the attainment of real sector development which is the underlying reason for its monetary stability mandate. The current positive MPR terrain puts MPC in a strong position to take a bold stance on monetary policy.

It is in the light of the above I hereby vote as follows: (1) to reduce MPR by 50 basis points to 11.50 percent with interest rate corridor of +/- 200 basis points; (2) to retain CRR at 12 percent; and (3) to retain Liquidity Ratio at 30 percent.

11.0 YAHAYA, SHEHU

I vote to maintain the Monetary Policy Rate at the current level of 12%. This is justified by the fact that there have been few fundamental developments since I voted to maintain the policy rate in January 2013. The two main changes that have occurred in the domestic economy do not, as yet, justify a change of stance.

At the global economy little has changed since January, except the recent upsurge in the stock markets. Growth has slowed to an estimated 3.2% from 3.9%. Growth is picking up in countries such as China, Brazil and Indonesia. It has also picked up a bit in the US, but may be negatively affected by the sharp cuts in government spending. Growth is robust in Africa and the Middle East, but the countries in these regions account, at the moment, for only a small proportion of the country's trade.

Although international oil prices are still high, there is a downward trend in January-February, a trend which is expected to continue in the next six months, not just because of the slow growth in the global economy, but also due to the massive increase in shale oil

production in US and Canada which will affect demand for Nigeria's Bonny light crude. Global prices are still on a downward trajectory.

In Nigeria, GDP is estimated to have grown at 6.58%, slightly below the projected growth rate and slower than 2011, although a slight pick-up is expected in Q1 of 2013. Growth is largely driven by the non-oil sector, while oil production declined in 2012. Food output prospects for 2013 are cautiously optimistic.

Reserves are at a healthy level of US\$49.4 billion, equivalent to 13 months of imports. The stock exchange has shown a significant rise in value and shares traded. However, much of the investment may be in the form of hot money. In the event of a significant reverse in portfolio investment therefore, this could have a deleterious effect on the level of reserves.

From the point of view of monetary policy, there are two main developments in the Nigerian economy since the January 2013 MPC meeting. The first is a surge in demand for foreign exchange

in the current month. Ordinarily, this can call for a tightening of monetary policy in order to ease the pressure and maintain the stability of the exchange rate around the policy band. However, I believe this challenge can be addressed through the judicious utilization of the reserves and open market operations.

The second development is more significant from the point of view of monetary policy- the decline of headline inflation rate to 9% in January 2013, which on the face of it may signal the creation of more room for easing monetary policy. However, the significance of this fall in headline inflation rate is undermined by the base effect of the high price levels emanating from the adjustment in fuel prices in January 2012. Furthermore there has been an upturn to 9.5% in headline inflation in February 2013. Food inflation (particularly farm produce) has also gone up. In addition, it is premature, on the basis of the figures for one month, or even two months, to determine that there is a fairly well established trend sufficient to justify a substantial change in policy.

The above position is strengthened by a consideration of the fiscal situation. There is no doubt that there has been a significant improvement in fiscal policy and implementation and greater prudence as compared to previous years. Nevertheless, some time is needed to study the effects of the implementation of the 2013 budget before its impact on spending and money supply can be properly gauged. This is particularly because the budget is predicated on a level of oil output that might be too optimistic. The surge of 18% in financial sector lending to the government sector in February 2013 (Year on Year), although by itself is not necessarily a bad thing, underlines the importance of carefully watching the trends on the fiscal side.

Unfortunately, there has been no decrease in interest rates charged by the Banks, and the gap between deposit and lending rates remains very wide, which obviously, in combination with other factors, makes it hard for SMES to borrow.

Overall, there is a high risk that easing monetary policy too early before an established downward trend of prices is established,

may generate inflationary pressures and Naira depreciation. At this time, this outweighs other considerations. I therefore vote to maintain the MPR and the Cash Reserve Requirement at the current level of 12%

12.0 SANUSI LAMIDO SANUSI, CON, GOVERNOR, CBN AND CHAIRMAN, MONETARY POLICY COMMITTEE

We are holding this meeting at a time when the global economic environment has not changed much since the last meeting. The IMF has revised its forecast of Global and Emerging Market growth in 2013 marginally downwards, but still projects an improvement over 2012. Emerging Asia is likely to continue showing resilience to global headwinds although a massive slowdown in Indian growth is a source of concern.

On the domestic front GDP growth in 2012 and projection for 2013 remain robust. As predicted, inflation figures have come down to single digits with headline Year-on-Year at 9.0% in January and 9.5% in February. A major reason for this outcome is the base effect of the first and second round inflationary impact of the partial removal of fuel subsidy in January, 2012. Inflation is

expected to remain in high single digits for most of the year, touching the 10% range at some points. Expectations are that the rate in March will be lower than February, but headline numbers will hover around 10% for the second and third quarters. This outcome reflects a combination of base effects, the impact of food harvest season, and continuing tight monetary policy stance.

There is no doubt that the monetary policy decisions taken by this committee over the past three years have turned out to be the correct ones, and have yielded desired outcomes. Inflation had actually come down to single digits at end of 2011 from around 16% in the early part of 2009. There is every reason to believe that without the oil subsidy price shock, 2012 would have witnessed a lower average inflation rate. Our decisions have reduced the inflation rate and, importantly, its volatility. We have also succeeded in stabilizing the exchange rate and keeping it within our target band. External Reserves have grown to almost \$50 billion on the back of high oil prices, exchange rate stability, and tight monetary stance (thus attracting significant portfolio flows into the capital markets).

Macro Risks

While recognizing the good work done in establishing stability on all fronts, we must recognize the inherent risks in the policy and strategy adopted. Reserves have grown to almost \$50b as indicated but an increasing percentage of reserve accretion comes from potentially volatile portfolio flows. In 2012 for example, out of the total capital imported of \$16.6 billion, only \$2 billion came in the form of FDI, compared to \$11.82 billion portfolio inflows into equities and \$1.66 billion into Bonds and money market instruments. In the first two months of the year capital importation amounted to about \$4.94 billion. Out of this 72.2 % was portfolio investment in the Equity market, 10.92 % in Bonds and 3.05 % in money market instruments (a total of 86.17 %). Only 9.52 % came in as equity FDI.

It is therefore important to always bear in mind the financial stability and sustainability implications of these flows. First, it is evident that the recovery of the Capital Market is driven, in large part, by those huge inflows. The problem is magnified by what, in

my view, was a pre-mature decision to increase the symmetric limit for daily stock price movement from 5 % to 10 %. While Capital Market regulators hold the view that this would improve the price discovery mechanism, engender trading efficiency and make the market less predictable, I believe that the decision, taken at a time of loose money in the advanced economies and significant “carry trade”, is at least partly aimed at fast-tracking the increase in the All-Share-Index. The potential to make up to 10 % gain in a single day attracts “hot-money” into the system and raises stock prices rapidly. But just as in 2008, this means the stock market would crash just as rapidly in the event of a reversal of flows. With reserves at \$49.3 billion out of which \$37.45 billion (or 75.8 %) is owned by the CBN, the macro risks are fairly well-mitigated. However the risks to the capital markets of an oil price shock cannot be ignored, and the CBN must ensure that banks comply with all the rules set up to ring-fence deposits and keep DMBs from taking bets on asset prices.

The point here is not to discourage foreign investment of any kind. Rather it is to point out that the skewed nature of the capital

imported toward equities is an indictment of government economic policy. These very low levels of FDI reflect failure to create conducive environment for long-term investment due to policy somersaults around PPPs and slow progress in power and oil industry reforms. The general deterioration in the security of life and property in the north, as well as an increasing sense of rising corruption and impunity also discourage investment.

The solution, therefore, is not to discourage portfolio flows or treat them as inherently undesirable, but to fast track the necessary improvements in governance and policy that will attract longer-term flows. We must keep reiterating that our decisions provide stability in the short-term but for long-term stability, fiscal retrenchment and structural reform are essential. If this is not done, there is no guarantee of sustaining the gains of monetary policy into the future.

Considerations

At this moment, however, we must acknowledge the successes of monetary policy and stress the importance of maintaining course.

With the approval of the 2013 budget based on an optimistic combination of price and output assumptions, the fiscal stance in 2013 will be unhelpful to monetary policy. To end the tightening cycle based on two months data and in the face of a relatively loose fiscal stance would in my view be pre-mature. It must be noted that although the fiscal authorities have indeed embarked on a part of consolidation, this high oil-price benchmark slows the pace of fiscal reforms.

The exchange rate has remained within our target range, even though it has come under relative pressure of recent. However this is not a cause for concern. With OBB and Interbank rates stuck to the lower end of our policy range for some weeks, there is scope for tightening using open market operations without breaching the ceiling of 14%. A combination of a structured use of OMO and interventions in the inter-bank market should keep the exchange rate within our range with no difficulty. There is no need for increasing MPR to address this situation, given the monetary space at our disposal.

Conclusion

I am not convinced that lowering MPR will lead to lower lending rates or higher GDP growth. I also think sending a signal of loosening at this point is premature in the face of the budget and exchange rate pressure. I also believe that if we maintain MPR and use OMO wisely, the market will correct itself and yields will rise to a level where the pressure on the naira is lifted once more.

In summary I believe we are in the right place and should remain there, while bearing in mind the risks highlighted above.

I vote for retaining the status quo.