



Central Bank of Nigeria Communiqué No. 105 of the Monetary Policy Committee Meeting of Monday and Tuesday, January 25 and 26, 2016

The Monetary Policy Committee met on 25th and 26th January, 2016 against the backdrop of weakening global economic prospects as well as increased risks in the domestic economic environment. In attendance at the meeting were 10 out of the 12 members. The Committee reviewed the ensuing international and domestic economic and financial environments in 2015 as well as the outlook for the first half of 2016.

On the global front, uncertainties and geopolitical tensions have increased in the Middle East, leading to a major standoff between two major oil producers; Saudi Arabia and Iran, in the face of improving relations between the United States (US) and Iran. In the global oil market, both Iran and the US are emerging as new suppliers while OPEC appears to have shifted from protecting price to defending market share. These developments underscore the conclusion that the current global oil prices would remain for a much longer period. Widespread stock market weaknesses and worsening macroeconomic conditions in China have further exacerbated the already stifling global economic challenges. These uncertainties have blended well with domestic vulnerabilities to affect the monetary policy environment in Nigeria.

International Economic Developments

The Committee noted the considerable divergence in global output recovery in 2015, as growth picked-up in the most advanced countries compared with slowdown in majority of emerging and developing economies. Following the slowdown in the emerging market economies, the IMF in its January 2016 World

Economic Outlook (WEO), revised its global growth estimate from 3.4 to 3.1 per cent and 3.4 per cent in 2015 and 2016, respectively.

In the United States, growth has remained relatively firm with 2015 third quarter growth rate revised to 2.1 per cent from an earlier estimate of 1.5 per cent. The country's overall growth in 2015 is expected to be the strongest since the post-crisis recovery began in 2010. Likewise, 2016 growth rate has been projected at 2.6 per cent. The major drivers of this growth remained improvements in consumption spending supported by a robust labor market recovery; low inflation stemming from soft global crude oil prices; massive and dynamic investments in the non-oil private sector, improved foreign investment demand due to the recent normalization of monetary policy by the Fed, as well as housing market recovery.

Japan's recovery in 2015 remained fragile despite the continuous policy stimulus by the Bank of Japan. The Bank's asset purchase program injects ¥6.7 trillion (\$56.71 billion) monthly into the economy, with the possibility of expansion. However, this has done little to restart growth which is estimated at 0.8 per cent in 2015. Private consumption and investment spending remained modest in 2015, worsened by rising skill shortages. Japan's outlook for 2016 remains dampened by the feeble response of the economy to monetary and fiscal stimuli.

In the Euro area, weakening fiscal consolidation and improving labor market conditions generated 1.5 per cent growth in 2015 with prospects for achieving 1.7 per cent in 2016. The European Central Bank (ECB) further eased its monetary policy stance in December 2015, despite the Bank's continuous monthly asset purchase of €60 billion (\$64.8 billion), as both inflation and wage growth remained subdued. In the same vein, the Bank of England continued its accommodative monetary policy through its £375 billion (\$540 billion) asset purchase program, even as it announced a decision to reinvest another £6.3 billion (\$9.07 billion), being the proceeds of redemption of the December 2015 gilt (government securities) held in the Asset Purchase Program. The Bank also maintained its core rate at 0.5 per cent in an attempt to herd inflation towards its target rate.

Growth in the emerging markets and developing economies (EMDEs) decelerated to 4.0 per cent in 2015, the lowest since 2009, as both external and domestic challenges continued; owing to low commodity prices, financial market volatility, slowing productivity, policy uncertainty and eroding policy buffers as well as weak global trade. The slowdown in the majority of EMDEs has also been attributed to spillovers from weaknesses in major emerging economies, diminishing capital inflows, rising borrowing costs and other geopolitical factors.

The stance of monetary policy in the advanced economies is expected to remain largely accommodative in 2016, except for the United States where monetary policy normalization has commenced. Against the background of suppressed commodity prices and slow recovery, global inflation is expected to remain moderate through 2016.

Domestic Economic and Financial Developments

Output

Domestic output growth in 2015 remained moderate. According to the National Bureau of Statistics (NBS), real GDP grew by 2.84 per cent in the third quarter of 2015, almost half a percentage point higher than the 2.35 per cent recorded in the second quarter. However, third quarter expansion remained substantially below the 3.96 and 6.23 per cent in the first quarter of 2015 and corresponding period of 2014, respectively. The major impetus to growth continued to come from the non-oil sector which grew by 3.05 per cent compared with the growth of 3.46 per cent posted in the preceding quarter. The major drivers of expansion in the non-oil sector were Services, Agriculture and Trade; contributing 1.42, 1.03 and 0.79 percentage points, respectively. The outlook for the fourth quarter of 2015, based on staff estimates, suggests further improvements over the third quarter growth level.

The economy is expected to continue on its growth path in the first quarter 2016, albeit less robust than in the corresponding period of 2015. This expectation is

predicated on the current low global oil price trend which is projected to hold low over the medium-to long term, and with attendant implications for government revenue and foreign exchange earnings. Other downside risks to growth in 2016 include: capital flow reversal, high lending rates, sluggish credit to private sector and bearish trends in the equities market.

However, the Committee remains optimistic about a gradual recovery in economic activity due to notable improvements in power and supply of refined petroleum products, improved policy recalibration aimed at improving the flow of financing resources to the real sector and suppression of internal insurgencies, which will boost general agricultural activity.

Prices

The Committee noted the slight uptick in year-on-year headline inflation to 9.6 per cent in December, from 9.4 per cent in November and 9.2 per cent in October, 2015. The increase in headline inflation in November 2015 reflected an increase in the food component, even though the core component remained unchanged at 8.70 per cent. Core inflation declined for the third consecutive month to 8.70 per cent in November and December from 8.74 per cent in October 2015, while food inflation inched up to 10.32 per cent from 10.13 and 10.2 per cent over the same period. Consistent with its primary mandate, the Committee would continue to monitor consumer price developments with a view to formulating policies that will keep inflation in check.

Monetary, Credit and Financial Markets Developments

Broad money supply (M2) rose by 5.90 per cent in December 2015, over the level at end-December 2014, although below the growth benchmark of 15.24 per cent for 2015. Net domestic credit (NDC) grew by 12.13 per cent in the same period, but remained below the provisional benchmark of 29.30 per cent for 2015. Growth in aggregate credit reflected mainly growth in credit to the Federal Government by 151.56 per cent in December 2015 compared with 145.74 per cent in the corresponding period of 2014. The renewed increase in credit to

government may be partly attributable to increased government borrowing to implement the 2015 supplementary budget.

During the period under review, money market interest rates generally reflected the level of liquidity in the banking system. Average inter-bank call and OBB rates, which stood at 1.00 and 1.50 per cent on 25 November 2015, closed at 4.75 and 4.50 per cent, respectively, on January 21, 2016. Between the November 2015 and end-December 2015, interbank call and OBB rates averaged 0.81 and 0.98 per cent, respectively.

The Committee noted the bearish movement in the equities segment of the capital market during the review period. The All-Share Index (ASI) decreased by 13.15 per cent from 27,435.56 on November 30, 2015 to 23,826.50 on January 22, 2016. Similarly, Market Capitalization (MC) fell by 13.06 per cent from N9.42 trillion to N8.19 trillion during the same period. However, relative to end-December 2014, the indices declined by 31.25 per cent and 28.66 per cent, respectively. This development reflected capital flow reversals accentuated by soft commodity prices and monetary policy normalization in the United States.

External Sector Developments

The Committee noted the ongoing activities in the informal segment of the foreign exchange market, which led to the stoppage of dollar sales to BDCs, even as the average naira exchange rate remained relatively stable at the inter-bank segment during the review period. The exchange rate at the interbank market opened at N197.00/US\$ and closed at N197.00, with a daily average of N196.99/US\$ between November 23 and January 11, 2015. The Committee underscored the necessity of improving the supply of foreign exchange to the market, especially from autonomous sources. It also reiterated its commitment to maintaining stability in the naira exchange rate.

Committee's Considerations

The Committee observed that the last episode of low oil prices in 2005 lasted for a maximum period of 8 months. However, the current episode of lower oil prices is projected to remain over a very long period. Consequently, it is imperative to brace up for a longer period of low government revenues from oil sources, which

would necessitate hard and uncomfortable choices as the economy transits to more sustainable sources of revenue, consistent with the economic realities and strategic objectives of the country. In the circumstance, certain tradeoffs must be envisaged and duly accommodated.

In view of the foregoing, the imperative for consistently sound and coordinated macroeconomic policy has become inevitable. In the medium term within which monetary policy is cast, the need to allow policy to produce the desired outcomes becomes a key consideration in the policy mix. Consequently, the Bank is fine-tuning the framework for foreign exchange management with a view to ensuring a more effective and liquid foreign exchange market, taking into account Nigeria's strategic development priorities; with the policies being designed within an environment of regularly ensuring consistency with monetary and fiscal policies.

The Committee noted that at its November 2015 meeting, it eased monetary policy with a view to increasing the liquidity of the banking system. This was aimed at moderating domestic interest rates so as to encourage indigenous businesses to borrow. While the objective of stabilizing the financial system in the aftermath of the Treasury Single Account (TSA) withdrawals and J. P. Morgan delisting of Nigeria have been largely achieved, the goal of increasing lending to key sectors of the economy is yet to be achieved as the Bank continues to adopt moral suasion to encourage the DMBs to support targeted lending to the real sector including agriculture, solid minerals and SMEs sub-sectors of the Nigerian economy.

Despite current challenges, the Committee remains guided by evidence underpinned by credible data in its holistic evaluation of the emerging scenario and in its assessment of policy choices. Consequently, the Committee believes that given sound and properly coordinated monetary, fiscal, and external sector policies, there is wide room for optimism about the medium to long term macroeconomic prospects for the Nigerian economy, especially, given the clarity in the policy direction of the administration, the various interventions in the real sector; gradual improvement in the power sector, and the reinvigorated fight against corruption. The Committee also believes that the effect of the softer

monetary policy stance adopted at the last MPC, should start crystalizing soon through expansion of credit to critical sectors of the economy. In addition, the unveiling of the Federal budget, oriented towards socio-economic and infrastructural development is expected to provide the necessary impetus for growth.

The Committee acknowledged the continuous liquidity surfeit in the system stemming partly from the recent growth-stimulating monetary policy measures, as well as the tendency of the banks to invest excess reserves in government securities, rather than extend credit to the needed sectors of the economy. To this end, the Committee once again urged the deposit money banks to improve lending to the real sector, as part of their patriotic obligations to the country and enjoined the Management of the Bank to continue to explore ways of incentivizing lending to employment- and growth-generating sectors, particularly SMEs.

The MPC also emphasized the necessity of coordination between monetary and fiscal policies as a prerequisite for resolving the nation's economic problems, particularly, steering the economy away from oil dependency. In particular, the Committee stressed the need for the fiscal authorities to compliment the Bank's low interest rate policy orientation by properly coordinating its borrowing activities (and rates) with the Bank in order to push the common objective of stimulating banking system credit delivery at low interest rates to the key sectors of the Nigerian economy. It noted that given the current economic reality of dwindling oil revenue and the rather unclear outlook for commodity prices, there would be need for a recalibration of the fiscal strategy to increasingly explore opportunities in non-oil tax revenue.

Finally, the Committee reiterated its unyielding commitment towards achieving a stable exchange rate regime to ensure more flexibility for sustainable inclusive economic growth in the medium to long term.

The Committee's Decisions

The Committee, in consideration of the headwinds in the domestic economy and the uncertainties in the global environment decided by a unanimous vote to retain the Monetary Policy Rate (MPR), Cash Reserve Requirement (CRR), Liquidity Ratio (LR) and the asymmetric corridor of +2/-7 around the MPR.

In summary, the MPC voted to retain:

- (i) the CRR at 20.0 per cent;
- (ii) MPR at 11.0 per cent;
- (iii) Liquidity Ratio at 30 per cent;
- (iii) The asymmetric corridor at +200 basis points and -700 basis points.

Thank you for listening.

Godwin I. Emefiele

Governor, Central Bank of Nigeria

26th January 2016