



CENTRAL BANK OF NIGERIA COMMUNIQUÉ NO. 127 OF THE MONETARY POLICY COMMITTEE MEETING OF MONDAY 25th AND TUESDAY 26th NOVEMBER 2019

The Monetary Policy Committee (MPC) met on the 25th and 26th of November 2019 in an environment of continued global macroeconomic uncertainty, but gradual improvements in the domestic economy. The Committee appraised the developments in both the global and domestic economies, as well as the outlook for the rest of the year and the first quarter of 2020. All the eleven (11) members of the Committee were in attendance.

The Committee reviewed the effect of monetary policy on developments in the economy in 2019, particularly, price stability, improved credit delivery, low interest rate regime, exchange rate stability, financial system stability, reduction in non-performing loans (NPLs), job creation and output growth.

The Committee noted the use of home-grown heterodox policies used by the Bank to successfully achieve substantial macroeconomic stability in 2019. Amongst the policies were the use of the Global Standing Instruction (GSI) to address the predatory impact of serial borrowers in the banking system, a phenomenon that reduced the level of NPLs over time, the Loan to Deposit Ratio (LDR) to boost credit delivery by the deposit money banks (DMBs) to the real sector, Differentiated Cash Reserve Requirement (DCRR), Development Finance Initiatives in agriculture, micro, small and medium enterprises (MSMEs) and other real sector activities, including restriction of patronage by local corporate and individual investors in CBN OMO bills.

Global Economic Developments

Global output growth remained weak due to the impact of the trade war between the US and China; growing vulnerabilities in the financial markets, downturn in global manufacturing, sustained downward pressure on oil prices, lingering uncertainty around BREXIT, which has continued to dampen

investment growth in the United Kingdom, subdued growth in the European Union and Japan, and dampening output growth in China. These headwinds resulted in slowing global trade, weakening aggregate demand and contraction in the aggregate supply chain. Major Emerging Market and Developing Economies (EMDEs) particularly China and India also slowed, while South Africa, Russia and Brazil, recorded slower-than-expected growth. Consequently, there was a broad slowdown in global output. In the light of these developments, the IMF revised global growth forecast downwards to 3.0 per cent in October 2019 from its previous projection of 3.2 per cent in July 2019.

Inflation in most Advanced Economies remained well below their long-run objectives, with price development staying subdued and unemployment trending mostly below the Non-Accelerating Inflation Rate of Unemployment (NAIRU). In the US, wage growth and aggregate demand continued to perform below the long run average even though unemployment remained below the NAIRU. Consequently, the recent trend towards monetary accommodation by key central banks is expected to continue into the foreseeable future. In key EMDEs, however, prices trended upwards with the output gaps widening and unemployment remaining relatively high.

Domestic Economic Developments

Data from the National Bureau of Statistics (NBS) showed that real Gross Domestic Product (GDP) grew by 2.28 per cent in the third quarter of 2019, compared with 2.12 and 1.81 per cent in the preceding and corresponding quarters, respectively. The improved growth was driven largely by the performance of the oil sector, which grew by 6.49 per cent, while the non-oil sector grew by 1.85 per cent. The Manufacturing and Non-Manufacturing Purchasing Managers' Indices (PMI) also expanded for the 31st and 30th consecutive months at 58.2 index points, apiece, in October 2019. Staff projections indicate that real GDP in Q4 2019 is expected to grow by 2.38 per cent, driven by the non-oil sector. Headwinds to this projection, include: continued high level of unemployment, mild resurgence of anticipated

inflationary pressures towards the December festive season, rising public debt, high level of insecurity, and slow pace of oil price recovery. Despite these headwinds, growth is expected to pick on the back of recent actions to boost credit to the private sector through the recent Loan-to-Deposit Ratio (LDR) and Global Standing Instruction (GSI) initiatives, sustained interventions by the Bank in selected employment and growth-enhancing sectors, as well as fiscal policy measures to support growth.

The Committee noted the uptick in headline inflation (year-on-year) from 11.24 in September to 11.61 per cent in October 2019. This was anticipated as part of the seasonal end-of-the year uptick in prices; but was further accentuated by the border closure, an expected temporary food supply shock which will adjust over the medium-to-long term as the economy increase investments in food production. Consequently, food inflation rose from 13.51 to 14.09 per cent in September and October 2019, respectively. Core inflation, the underlying inflation in the economy, however, declined marginally from 8.94 to 8.88 per cent in September and October, respectively. The decline observed in core inflation was attributed to the relative stability in the foreign exchange market. The Nigerian land borders were closed to address the incidence of increased cross-border banditry, smuggling and dumping, insurgency and the illegal trade practices of neighbouring countries whose economies had become dependent on Nigeria through smuggling through the borders. The Bank's continued intervention in the agricultural sector is expected to improve medium-term food supply. Indeed, there has been reports of bumper harvest in some staples like rice, maize, etc.

The Committee observed that broad money supply (M3) grew by 5.72 per cent (year-to-date) in October 2019, compared with the 2019 indicative benchmark of 16.08 per cent. Growth in Net Domestic Credit (NDC) moderated to 26.38 per cent in October 2019 from 30.33 per cent in the previous month. This was attributed to a significant reduction in credit to Government in October 2019 to 85.99 per cent from 114.79 per cent in the previous month. Growth in credit to the private sector, however, improved to 13.08 per cent in October 2019 from 12.49 per cent in the previous month,

reflecting the impact of the Bank's recent policy on loan-to-deposit ratio. An increase in absolute gross credit, amounting to N1,169.70 billion, was recorded between end-May and end-October 2019. Consequently, the manufacturing sector received N459.69 billion, the highest in two decades. This was followed by consumer loans of N356.65 billion, General Commerce (N142.98 billion), Information and Communications (N82.07 billion), Construction (N74.52 billion), Agriculture, Forestry and Fishing (N73.20 billion), Mining and Quarrying (N3.64 billion) and Transportation and Storage (N3.09 billion), amongst others. The Committee, therefore, urged the Management of the Bank to sustain its current efforts to improve lending to the private sector and to explore other initiatives to provide funding to other critical sectors of the Nigerian economy.

In the review period, money market interest rates reflected the prevailing liquidity conditions in the banking system. Overall, the monthly weighted average Inter-bank call and Open Buy Back (OBB) rates fell to 7.87 and 7.22 per cent, respectively, in October 2019, from 11.41 and 10.73 per cent, respectively, in September 2019.

The Committee noted that the persisting bearish trend in the equities market, had started to abate in November 2019, and was pleased by the increased patronage in the sovereign bonds market. The All-Share Index (ASI) grew by 2.41 per cent to 26,991.42 index points on November 22, 2019, from 26,355.35 index points at end-October 2019. Market Capitalization (MC) also grew by 1.54 per cent to N13.03 trillion on November 22, 2019, from N12.83 trillion at end-October 2018, due largely to portfolio shift from short-term Government securities to the equities market.

The MPC also noted the improved resilience of the banking system, as the Non-Performing Loans (NPLs) ratio declined further to 6.56 per cent at end-October 2019 from 6.67 per cent at end-September 2019 and from 14.05 per cent in October 2018. The Committee, however, noted that this figure remained above the prudential benchmark of 5.0 per cent, and urged the Bank to sustain its current efforts, which have created this exorable prudential regime.

Outlook

Overall, the medium-term outlook for the domestic and global economies continue to be clouded with uncertainties, associated with the persisting trade wars between the US and its major trading partners, financial vulnerabilities, rising levels of public and corporate debts, pockets of geopolitical tensions and weakening global output. However, the reforms underway in the domestic economy; aimed at diversification away from oil over the last three years have provided adequate shock absorber to withstand the headwinds. However, the Committee urged the fiscal authorities to invest massively in public works programme and improve fiscal buffers to complement these efforts.

Forecasts of key macroeconomic variables, however, indicate prospects of improved output growth for the economy. Based on recent revised projections, the economy is expected to grow in 2019 by 2.3 per cent (IMF estimate), 2.1 per cent by the World Bank, and 2.20 per cent by the CBN. The Committee noted the tailwinds to these developments, to include: sustained stable exchange rate; enhanced flow of credit from the Deposit Money Banks (DMBs) to the private sector; expected improvements in tax revenue and efficiency in public expenditure; continued improvement in the business environment and activities; and the sustained interventions by the Bank in the real sector.

The Committee's Considerations

The Committee welcomed the improvements in output growth in the third quarter of 2019, noting that the current direction of the Purchasing Managers Index suggests stronger growth in the fourth quarter. It however, re-emphasized the need for diversification to strengthen the productive base of the economy and reduce dependence on oil. Diversification has become necessary now that Nigeria has signed the African Continental Free Trade Agreement (AfCTA). To achieve this, the Committee urged the Federal Government to continue to improve the investment climate and ease of doing business to attract Foreign Direct Investment. Particularly, Government should, as a

priority, improve conditions for global auto manufacturers, including for aviation and rail industries to invest in the country.

The Committee commended the expansion in manufacturing output, noting that it was a direct fallout of the policy on loan-to-deposit ratio. The Committee, called on Government to urge the Pensions Commission to improve the prudential requirements for Pension Funds to refocus their investment portfolio away from their traditional choice of Government securities in favour of other viable long-term investments in real estate, manufacturing and agriculture; and indeed infrastructure. Moreover, the Committee called for strong visibility of fiscal and structural policies to improve infrastructure and investment conditions in the economy. It expressed strong optimism that the current policies of the Bank, in a regime of solid fiscal and structural policy support, would yield strong dividends in closing the current negative output gap in the medium to long term, and place the economy on a sustainable and self-sufficient path of output growth.

As a key pillar of economic diversification, the MPC directed the attention of the fiscal authorities to the immense potentials of the gas sub-sector and the urgency to encourage horizontal integration through private sector participation. This, the Committee argued will improve domestic power supply and export earnings.

On price developments, the Committee considered the moderate uptick in headline inflation in October 2019, attributing it partly to an expected temporary shortfall in food supply because of the recent land border closure and rise in demand as the festive season approaches. Although it noted that the price increase was not unexpected, the Committee believed that the medium to long-term benefits far outweigh the short-term cost. Consequently, it noted the need to drive down food prices through increased support for local production of staples foods, including rice, fish, poultry, palm oil, tomatoes etc. It also urged the Government to follow through with a sustainable policy on backward integration in the milk industry and other priority sectors of the economy.

On the fiscal sector, the Committee identified the need for institutional reforms through policies that would automate day to day processes of key revenue generating and security agencies such as the Nigerian Customs. This would provide additional advantage of stemming smuggling, kidnapping and the migration of terrorists into the country. The MPC reiterated the need for increased efficiency in public expenditure and the building of fiscal buffers.

On the impact of the recent closure of Nigerian land borders on domestic food prices, the Committee noted that any upward price movement arising from the closure was reactionary and therefore temporary. Moreover, significant investment has been made over the last three years to sustainably increase domestic food supply. It noted some of the key initiatives in this direction to include: the Commodity Development Initiatives, designed to finance the agricultural value chain of ten ((10) commodities namely; Cassava, Cocoa, Cotton, Rice, Tomato, Poultry, Livestock and Dairy, Fish, Oil Palm and Maize, which has received N171.66 billion in funding. Four of these crops received over 140.12 billion naira or 81.6 per cent of total disbursements (Cassava, 11.44 billion naira; Cotton, 40.47 billion naira; Rice, 53.40 billion naira; Oil palm, 34.81 billion naira). It is, therefore, expected that the outcome of these interventions will close the supply gaps already envisaged in the medium to long term, including dampening domestic prices. It thus, expressed support for the temporal closure of Nigeria's land borders, noting that securing the country's land borders should be further enhanced.

On crude oil price, the Committee noted the lull in the futures market, suggesting that prices would remain relatively weak into the foreseeable future. The Committee, therefore, urged the Federal Government to reconsider its 2020 budget oil price benchmark of US\$57 per barrel, to build fiscal buffers.

The Committee was confident that despite the weaknesses from the external sector, efforts to ramp-up domestic production, through several measures by both the monetary and fiscal authorities, would douse the adverse effects on the domestic economy in the medium term, through the reduction of importation of food and other commodities.

The Committee's Decision

The MPC reviewed the upsides and the downsides of the options to tighten, hold or loosen. It was conscious that, while tightening may encourage capital inflows, it also has the downside consequence of constraining the already nascent recovery in output growth. The Committee also noted that a reduction in the policy rate will improve growth prospects, but in view of the uptick in inflationary pressures, it decided that the balance of risks was in favour of protecting price stability. Considering the recovery, decline in market interest rates, growth in domestic credit amongst other positive developments, the Committee felt that there would be more gains in the short to medium term in holding policy at its current position.

In its consideration to hold, the MPC noted with pleasure, the positive outcome of actions already taken by the Bank. These actions include: current policy on loan-to-deposit ratio, which has resulted in loans and advances rising by over N1.1 trillion between June to October 2019. It further noted that these actions have assisted in boosting credit to the agricultural and manufacturing sectors, hence, the positive outcome on the GDP. The MPC is hopeful that the LDR initiative must be sustained as interest rates being paid by borrowers have so far dropped by up to 400 basis points between June and October 2019. These have happened with corresponding decline in NPLs to 6.5 per cent at end-October 2019. The MPC is, therefore, of the view that sustaining the MPR at its current level is crucial for better understanding of the unfolding impetus of growth before deciding on any probable variations. The MPC also feels that holding its current policy position offers pathways for appraising the effect of the heterodox policies to encourage lending by the banking industry without varying the policy rate as the downside risk to growth and caution on inflation looks stable. The MPC is also of the view that the improvements in the macroeconomic indicators such as the GDP, NPLs, CAR, and the LDR, suggest that current monetary policy stance is yielding results. It therefore, feels that maintaining the current stance would be necessary in order to sustain the improvements.

In view of the foregoing, the Committee decided by a unanimous vote to retain the Monetary Policy Rate (MPR) at 13.5 per cent and to hold all other policy parameters constant.

In summary, the MPC voted to:

- I. Retain the MPR at 13.5 per cent;
- II. Retain the asymmetric corridor at +200/-500 basis points around the MPR;
- III. Retain the CRR at 22.5 per cent; and
- IV. Retain the Liquidity Ratio at 30 per cent.

Thank you.

Godwin I. Emefiele
Governor, Central Bank of Nigeria
26th November 2019