

Central Bank of Nigeria Communiqué No. 89 of the Monetary Policy Committee Meeting of Monday and Tuesday, May 20 and 21, 2013

The Monetary Policy Committee met on May 20 and 21, 2013 with 10 out of the 11 members in attendance. The Committee reviewed the conditions and challenges that confronted the domestic economy in the first five months of 2013, and reassessed the short-to-medium term monetary policy options in the light of the fragile global economic and financial environment. The Committee noted that one of the members, Professor Sam Olofin has left the Board of the Central Bank and, therefore, ceases to be a member of the MPC. The Committee recognized his tremendous contributions to its deliberations over the years and thanked him for his services.

International Economic Developments

Global economic recovery continues to be fragile due to suppressed growth and weakness in key financial markets, including the euro area and Japan. However, the emerging market economies and Sub-Sahara African (SSA) countries continued to show resilience.

Global growth outlook remains subdued but promising. It is forecast to average 3.2 per cent in 2013. In the advanced economies, output is estimated to grow by 1.2 per cent in 2013 compared with 1.3 per cent in 2012. In the US, budget deficit figures are better than projections due to automatic spending cuts and improved revenues boosted by dividend payments to the Treasury from mortgage banks bailed out during the crisis. Unemployment figures are also improving. Although the European Central Bank has commenced a wave of monetary easing, the euro area is expected to remain in recession with output contracting by 0.3 per cent compared with a contraction of 0.6 per cent in 2012. The EU made steady progress in establishing a Banking Union, pursuing a

three-pronged initiative of the Single Supervisory Mechanism; Deposit Guarantee System; and a Recovery and Resolution Scheme. The development has been adjudged as an important step towards recovery. The regime of quantitative easing commenced by the Bank of Japan holds prospects for Japanese recovery arising from a weaker Yen and improved competitiveness of Japanese exports. However, the downside risk lies in Japan's demographics whose key feature is a low propensity to consume, given its large population of pensioners-about 30 per cent. With slowing growth momentum in the emerging markets, global output is forecast to remain around the 2012 level.

The emerging and developing economies as a group are forecast to grow by 5.3 per cent in 2013, with SSA growing at 5.6 per cent. These economies have continued to face the challenge of adjusting macroeconomic policy to compensate for the weak external environment, particularly shocks induced by developments in the advanced economies. The IMF suggests that with the prospects of improvements in the global economy, policy recalibration in a number of emerging market economies should address risks from sustained rapid credit expansion and high asset prices. Growth in these economies has somewhat moderated compared with last year. The strong GDP growth rate of 7.7 per cent recorded in the first quarter of 2013 for China was countered by weaker rates in the other economies.

Domestic Economic and Financial Developments

Output

The National Bureau of Statistics (NBS) forecasts real GDP growth rate of 6.72 per cent for Q2, 2013, an improvement over the Q1 estimate of 6.58 per cent. The major driver of overall growth remains the non-oil sector led by services; agriculture; and wholesale and retail trade. The Committee noted that the relatively robust output growth projection for 2013 was hinged on expected

favourable conditions for increased agricultural production and other policy initiatives aimed at stimulating the economy. However, the Committee noted with caution, the high GDP growth projection in view of the extant risk factors such as widespread insecurity, weak infrastructure and probable flooding from the projected heavy rains in some parts of the country. In addition, the state of emergency in the North East and the accompanying military operations in that axis have the potential to adversely affect economic activities generally, including agricultural production and food prices, as well as consumer demand. The Committee also noted that although most sectors of the economy showed improved growth performance in Q1 of 2013 when compared with Q1 2012, this was not the case with respect to the key sectors like agriculture, telecommunications and distributive trade. Concern was also expressed over short-term prospects in the oil sector, mainly around possible reduction in oil prices and continuing leakages in oil production due to bunkering and other illegal activities.

Prices

Headline inflation increased from 8.6 per cent in March to 9.1 per cent in April, remaining within the target range for the fourth consecutive month. Food inflation was 10.0 per cent year-on-year in April compared with 9.5 per cent in March, while core inflation declined further to 6.9 per cent from 7.2 per cent in March. On a month-on-month basis, inflation showed broad-based moderation across almost all components with the exception of imported food which may be largely a reflection of the new tariff regime.

The inflation outlook remains relatively benign with projections of headline inflation remaining in the single digit range for the next six months. This result reflects a combination of base effect and the success of tight monetary policy leading to muted growth in the monetary aggregates and exchange rate

stability. The principal risks to the outlook remain fiscal spending and possible pressures on the exchange rate from any attrition to reserves caused by declining revenues as a result of output leakages.

Monetary, Credit and Financial Market Developments

Broad money supply (M2) grew by 4.44 per cent in April 2013 over the level at end-December 2012. When annualised, M2 grew by 13.3 per cent, compared with the contraction of 0.03 per cent in the corresponding period of 2012. The growth in M2 was slightly below the growth benchmark of 15.2 per cent for 2013. Aggregate domestic credit (net) grew by 17.46 per cent in April 2013 which annualized to a growth rate of 52.38 per cent over the end-December 2012 level, compared with the contraction of 6.12 per cent recorded in the corresponding period of 2012.

Interest rates in the interbank money market moved in tandem with the level of liquidity in the banking system. The average inter-bank call and OBB rates which opened at 10.21 and 10.23 per cent on March 19 closed at 10.86 and 10.91 per cent, respectively, on May 16, 2013. The average maximum lending rate rose marginally to 24.53 per cent in April, 2013 from 24.49 per cent in March, 2013. Similarly, the average prime lending rate, rose to 16.65 per cent in April 2013, from 16.61 per cent in March.

The Committee noted the continued recovery in the Nigerian capital market as equities market indicators were positive in the review period. The All-Share Index (ASI) increased by 31.4 per cent from 28,078.81 on December 31, 2012 to 36,907.81 on May 17, 2013. Market Capitalization (MC) also increased by 31.5 per cent from N8.97 trillion to N11.80 trillion during the same period. Improved earnings, increased capital inflow and portfolio investments as well as investor confidence in the economy contributed to the up-swing in stock prices. The Committee also noted the reported increase in the share of domestic players in

the capital market, thus reducing the risk of major shocks due to slowdown in foreign participation.

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 N157.32/US\$, N158.70/US\$, and N160.00/US\$ on 20th March 2013 and closed at N157.30/US\$, N158.33/US\$, and N159.50/US\$, respectively, on May 18, 2013. In all three segments, the naira exchange rate appreciated in the review period. This development reflected the effects of improved supply of foreign exchange to the market. Both the average and monthly premia for the review period remained insignificant, indicating the effectiveness of current policy measures.

The Committee also expressed satisfaction with the significant accretion to external reserves which stood at US\$49.13 billion as at May 16, 2013. This represents an increase of US\$5.3 billion or 12.1 per cent above the level of US\$43.83 billion at end-December 2012. This level of reserves could finance approximately 13 months of import.

The Committee's Considerations

The Committee was pleased with the prevailing macroeconomic stability-moderation in all measures of inflation on month-on-month basis; stable banking system and exchange rate and robust external reserves. It commended the agreement reached between the CBN and AMCON on the settlement of outstanding AMCON obligations to all private sector investors by December 2014 and to repay the N3.6 trillion debts held by the CBN under a new refinancing and restructuring arrangement within a period not exceeding ten years at single-digit interest rate. The Committee noted that the repayments and refinancing arrangements would have no adverse monetary policy implications;

but rather increase confidence in the financial system. Also, under this arrangement, it is unlikely that banks will be required to contribute more than 0.5 per cent of their Balance Sheets annually to the sinking fund. By October 2014, the CBN will be the sole creditor to AMCON, holding bonds guaranteed by the Federal Government of Nigeria. The Federal Government will therefore have no contingent liability to any party other than the CBN, and the Bank will recover its debt from AMCON recoveries and contributions to the Sinking Fund by the banks. Since the CBN supervises and regulates the banks and AMCON, this exposure is considered a fair risk.

The Committee was concerned about the threat posed by developments in the oil sector arising from uncertain oil market environment, high output leakages arising from oil theft which has negatively affected the oil sector's contribution to GDP and the prospects for declining output if the state of affairs continues. The Committee observed that the accretion to reserves resulted principally from increased portfolio capital inflows. The Committee noted the potential effect of this development on exchange rates, reserves and the capital account in the event of capital flow reversal, and thus stressed the need to maintain stability and retain confidence of investors in the consistency of monetary policy.

The Committee also expressed concern over the low level of credit growth to the private sector and traced this to the crowding out effect of high growth in credit to the public sector. The Committee noted the N1.02 trillion increase in claims on government and the N1.11 trillion drawdown on savings between January and April 2013 and particularly the monetization of US\$1 billion in April 2013, being proceeds of the Excess Crude Account. The combined effect of new borrowings and reduced savings was an increase in net credit to the central government of over N2 trillion in the first four months of 2013. The evidence points to an increase in the rate of government expenditure in 2013

when compared with 2012. In addition, the recent military action in the North-East will result in additional spending. Although the Government has announced that there will be no supplementary budget, the Coordinating Minister for the Economy and Honorable Minister of Finance has already announced that there will be a drawdown on a Contingency Vote embedded in the 2013 Budget to cover emergencies. Overall, the Committee is of the view that government spending will constitute a major risk to the inflation and exchange rate outlook, thus advising prudence in monetary policy action at this time.

The Committee further noted that in spite of increased borrowings, yields on FGN bonds have been declining steadily, signaling the impact of increased inflows while equity prices have been trending upwards. The evidence does not, therefore, support claims of monetary policy being too tight. The Committee was of the view that the principal risks to long-term stability can be addressed through diligent implementation of sound policies of fiscal consolidation and efficient sectoral policies underpinned by structural reforms. These are required to attract long term foreign capital inflow that would make the gains of monetary policy sustainable, and also support credit extension to the private sector players.

Consequently, the Committee weighed the following options:

(i) A reduction in rates in view of declining core inflation, stable exchange rates and relative reserve accretion. Against the backdrop of sustained pressure to ease the stance of monetary policy, the Committee considered the imperative of signaling its sensitivity to the concerns expressed about high lending rates in the economy;

(ii) Retaining current monetary policy stance to sustain the macroeconomic gains of tight monetary policy and to continue to rein-in inflationary expectations.

The Committee's Decisions

The Committee considered and acknowledged the merits of option 1 but rejected it as being premature in view of the potential risk factors in the horizon posed by recent developments which would necessitate increased fiscal expenditure in the short-to-medium term, resulting in a resurgence of inflationary pressures. The Committee considered and decided by a majority of 7 votes to hold and 3 votes to reduce the MPR by 50 basis points. Thus, by a majority vote of 7 members to 3, the MPC voted to maintain the current policy stance i.e. retain the MPR at 12 per cent with a corridor of +/-200 basis points around the MPR; retain the Cash Reserve Requirement at 12 per cent and Liquidity Ratio at 30 per cent; with the Net Open Position at 1.0 per cent.

In the final analysis, the Committee was convinced that in view of the successes achieved in all fronts - banking stability, low inflation, exchange rate stability, strong reserve buffers and recovery in the equities market, there is no reason at this point to change a policy that has worked so well.

Thank you.

Sanusi Lamido Sanusi, CON

Governor

Central Bank of Nigeria

21st May 2013

PERSONAL STATEMENTS BY MPC MEMBERS

1.0 ALADE, SARAH

Headline inflation increased to 9.1 percent in April from 8.6 percent recorded in March, 2013. This increase is due to a combination of base effect of the partial oil subsidy removal in 2012; and the dwindling of local food supply as planting season commence, suggesting that inflation may be expected to stay elevated in the coming months. In the international scene, there are some bright spots, but overall, growth remains subdued with implication for spillover on the Nigeria economy in terms of export earnings, exchange rate stability and reserve build-up. On the domestic front, first quarter GDP grew by 6.6 percent compared to 6.9 percent recorded in the last quarter of 2012. Based on this mixed developments, I am inclined to support a hold in Monetary Policy Rate (MPR) and Cash Reserve Requirement (CRR).

There are some bright spots in the global scene, but some weaknesses remain. The Eurozone economies are in the longest recession since record began in 1995. Gross Domestic Product (GDP) for seventeen countries using the euro fell for the sixth straight quarters in a row to -0.2 percent, although it is an improvement from -0.6 percent recorded in last quarter of 2012, but it is still a 1 percent annual contraction in GDP growth. This is as a result of reduced government expenditure and tax increases. Germany which contribute more than a third of euro zone's economic output grew by a weaker than expected 0.1 percent in the first quarter. As a major trading partner, this has implication for the Nigeria economy in terms of export earnings and reserve build-up. Although the European Central Bank predicts slow recovery in the coming months, there are still many risks to this prediction. In the United States, the effect of fiscal consolidation is being felt in many areas, although latest unemployment data is positive. These mixed development calls for a cautious approach to monetary policy until condition stabilizes.

The achievement of single digit inflation should be taken with cautious optimism. The decrease in inflation numbers to single digit in four straight months is a laudable achievement. This is a welcoming development, signifying the benefit of past monetary policy actions and overall policy coordination that has helped sustain the improved macroeconomic environment. While this development coupled with high reserve build-up present a strong argument for monetary easing at this point, especially to aid credit creation and flows to real sector of the economy, there are also compelling arguments for retaining the current stance given that inflation edged up to 9.1 percent in April from 8.6 percent in March, suggesting that the threat of inflationary pressure still looms on the horizon. In addition, it is important to recognize that there is a limit to the efficacy of monetary policy in terms of credit flow to the real sector, since structural imbalance in the economy plays a major role. In addition, with downside risks such as depressed global growth and uncertainties in the domestic economy, a rushed monetary easing may not be in the interest of economic stability. Furthermore, the start of the planting season is expected to further put upward pressure on domestic food prices and overall headline inflation in the coming months, as consumable supplies dwindle, suggesting that the inflation outlook in the coming months may not be completely benign.

Domestic output is trending downwards. The 2013 first quarter GDP grew by 6.6 percent as against 6.99 percent recorded in the fourth quarter of 2012. Non-oil sector grew by 7.9 percent compared to its contribution of 8.2 percent in the fourth quarter of 2012. The oil sector's contribution to GDP declined by -0.5 percent in the first quarter as against a decline of -0.2 percent decline in the last quarter of 2012. These developments can be attributed to a combination of insecurity in the northern part of the country that has affected agricultural production and oil theft and pipeline vandalism in the Niger Delta. Although National Bureau of Statistics (NBS) projections suggest a GDP growth of 6.75 percent for the year, however, the achievement of this

goal will require careful planning and maintenance of stable macroeconomic environment.

Money market conditions suggest ample liquidity in the banking system. While money market rates have increased from the rates obtainable before the last Monetary Policy Committee (MPC) meeting of March, 2013, great effort have been employed by the Central Bank to achieve these rates through frequent Open Market Operations (OMO) auctions. CBN securities worth N8.830.00 billion were offered between January 2 and May 17, 2013, and this amount was substantially oversubscribed, suggesting excess liquidity in the system. Growth in aggregate money resulted in a decline in maximum lending rate to 22.3 percent in April from an average of 25 percent in the first three months of the year. This development coupled with anticipated upward inflationary pressure would suggest that monetary easing at this time may be counterproductive.

Oil output and production are hovering below projections while international oil price is starting to trend downwards. The continued slow-down in global growth and increased domestic oil production in the United States is affecting global oil prices and demand. Oil output in the 2013 is lower than budgeted as a result of pipeline vandalism and oil theft, in addition to downward trend in oil prices in recent months. Overall production in the first quarter of 2013 remained below 2012 average production. According to WEO, April 2013 report, average crude oil prices fell by 3.7 percent in April to \$98.9 per barrel on weak demand, higher stocks and continued gains in supply. If this trend persist, it would 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 exchange rate. In the face such risk, monetary policy should do all it can to dampen the adverse effects on the economy.

Base on the above, I recommend a hold on Monetary Policy Rate and Cash Reserve Requirement (CRR), to consolidate on the macroeconomic gains.

2.0 BARAU, SULEIMAN

1.0 Review of Developments

- 1.1 Year-on-Year (YoY) Headline Inflation increased marginally to 9.1 per cent in April from 8.6 per cent in March on account of declining food inventories. It gives comfort that this is the fourth consecutive month of single digit in the all-items measure of inflation in several years. However, one should also observe that the marginal increase may indicate a trend toward double digit. YoY Food Inflation also trended marginally upward to 10.01 from 9.48 per cent in April and March, respectively. Core Inflation trended downward to 6.9 from 7.2 per cent over the same period.
- 1.2 Money Market rates have been stable albeit showing a marginal decline in April due largely to the sustained liquidity in the banking system. The spread between deposit and lending rates remain high; estimated at an average of 19 per cent.
- 1.3 The Naira exchange rate remained stable, while showing marginal appreciation in the three market segments. The wholesale Dutch Auction System (wDAS) rate appreciated marginally by 0.01 per cent to N157.20/US Dollar (17/5/13) from N157.32 (18/3/13).
- 1.4 Estimated GDP growth at 6.56 per cent remains robust though it trended downward compared with Q4 of 2013 of 6.99 per cent. This level of growth is however high when compared to Q1 of 2012 (6.34%). Besides, current GDP estimates and outlook is impressive when compared with Sub-Saharan African average.

- 1.5 Oil prices are trending downwards. Nigeria's Bonny Light at \$105/pb as at end April is dangerously trending towards the \$100 resistance level. This is lower than the average of \$113.7 in 2012. The days of rally in oil prices is now somewhat over.
- 1.6 Foreign Reserves is stable at \$47.9billion in April. This is inspite of the slow-down of foreign portfolio inflows, a reduction in oil price and oil production and export levels. Foreign Reserve level as at 13/4/13 is higher than the average for Q2.
- 1.7 Oil production levels have trended downward to an average of 1.9 million barrels per day (mbpd) in March and April compared to the average of 2.0mbpd in 2012 due largely to increased production leakages.
- 1.8 The banking industry has remained substantially liquid. Average liquidity ratio stood at 72.4 per cent as at end-April compared with 60.8 per cent as at end-December, 2012
- 1.9 In the area of public finance, at Federal level, we have seen remarkable reduction in revenues accruing to government due to reduction in oil production. But we have also seen remarkable increase in expenditure which translated into higher deficit of N236 billion which is 6.4 per cent higher than budgeted deficit of N222 billion.
- 1.10 There was remarkable growth in the banking industry balance sheet to N21.2 trillion as at 13th April, 2013 compared to N18.61 trillion as at April 12, 2012. There was corresponding increase in gross credit of 14.2 Year-on-Year in April, 2013.
- 1.11 In summary we have seen the monetary and financial stability due to the following key developments since the last MPC.

- Stability in prices – interest and foreign exchange
- Stable (Headline) inflation in the last four months with mild increase in inflation from March to April
- Stable but increasing foreign exchange reserve levels
- Declining oil price, government revenue and increase in Federal Government deficits relative to budgeted levels.
- Robust but declining GDP growth rate for Q1 2013 when compared with Q4 2012. GDP growth rate for Q1 2013 is however higher than that of Q1 2012.
- Decline in lending to the manufacturing sector in 2013 compared to 2012 but we have also seen increased overall lending to private sector. We have seen crowding out of private sector by public sector borrowing.
- Substantial liquidity in the banking system

2.0 Outlook/Risk/Considerations

- 2.1 Fiscal spending. I clearly see elevated risk to inflation and exchange rate due to the possibility of increased Government spending particularly as we seek to resolve the security challenges in the North-Eastern part of the country. We are also likely to see increased spending in the second part of 2013 as we head into the pre-election year.
- 2.2 Sustained liquidity in the banking system which will support the potential increase in Government spending. This would pose further risk to inflation and exchange rate management.

- 2.3 GDP growth continued to be robust as a result of the observed weak link between interest rate and private sector credit growth. This may continue until we see fundamental structural reforms in the real sector.
- 2.4 Declining oil price and export volumes is a major threat to foreign reserves accretion, exchange rate and government revenues. Lower government revenues would potentially translate into increased borrowing (and further) crowding out of the private sector and increase in borrowing rates. Declining oil price has the potential, if not managed, in reducing foreign reserves. This will negatively impact our exchange rate management
- 3.0 Monetary policy decisions should necessarily be forward looking. The current clamour for easing monetary policy is based on the gains made in tackling inflation, stability in interest rate and exchange rate, and accretion to reserves, amongst others. The clamour does not take into account the risks to these modest gains in changing policy stance to these variables. I am convinced that what we need is stability, to enable us to build on these gains rather than risk losing them by changing stance of monetary policy. The need to see increase in lending to the real sector is strongly desired but the risk of easing may appear even higher. Besides, we have witnessed strong growth inspite of the current tight stance in policy. It is yet to be proven that without structural reforms, we would elicit increased lending to the private sector and higher growth level, if we ease policy.
- 4.0 It is in view of the foregoing that I vote to hold current stance in policy by;
- Maintaining MPR at 12%
 - Maintaining the corridor at + and -2% around MPR

- Maintaining Cash Reserve Ratio (CRR) at 12%
- Maintaining Net Open Position (NOP) at 1% of Shareholders Funds

3.0 GARBA, ABDUL-GANIYU

Decision

1. I vote to:

- i. Reduce the MPR by 0.50% to 11.50%.
- ii. Maintain the asymmetric corridors at $\pm 2.0\%$ around the MPR.
- iii. Maintain CRR at 12%.

The Context of the Decision

2. I have consistently voted for a rate cut since January, 2013. My vote for cutting MPR in January was to signal “a commitment to macroeconomic stability now and, in the future and, to avoid history repeating itself at an even greater cost” also, 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.”
3. My conviction then (January and March) and now is that price stability must be conducive to job creating growth.
4. My key concerns then and now include (a) the co-existence of record stock market indexes, record growth in sovereign debts and persistent high unemployment; (b) the rising economic costs of achieving price stability through sustained tightening under an expansionary fiscal regime; (c) the infectious/competitive rounds of quantitative easing by the US Federal Reserve Board, the European Central Bank, the Bank of England and the Bank of Japan and the exports of short to medium term costs to Nigeria

(inflation through depreciation of the US\$, volatile financial flows and costly policy trade-offs) and, (d) the risks of currency wars, asset price bubbles, exportation of inflation and new rounds of financial and macroeconomic crisis as the major Central Banks persist in printing their way to growth and lower levels of unemployment.

5. I am still convinced that the global economy is fragile given (a) the fundamentals of the global economy, (b) the medium to long term costs of quantitative easing by the main Central Bankers and (c) the dis-equilibriums, asymmetries and inefficiencies in the dominant global financial games. As I argued in my personal statement in March, in a strategic, asymmetrical and volatile interdependent situation, the best strategy for public policy makers is a forward looking one empowered by continuous monitoring and analysis of economies, of financial games and of strategic players. Nigeria's urgent needs give such a strategy much supports and make creative and harmonious monetary and fiscal reaction functions critically important.
6. The comprehensive analysis of available data (inflation, interest rates, money survey, fiscal deficit, public debt, banking system and corporate financials, capital importation, All Share Index, Market Capitalization) for the period 2000-2013 preparatory to the meeting convinced me more than ever that a forward looking strategy is the best for these times.

The Basis for Decision

7. In weighing the arguments for holding against the argument for rate cuts, I asked myself if (a) the basis for my decisions in January and March have changed and (2) if my decisions were wrong. On both counts I have not established new facts that cause me to alter my decision.

8. Reserves are improving, the exchange rate remains stable and staff estimates forecast inflations to trend downwards. Obviously, the argument for rate cuts is strengthening not weakening. It is true that tightening has worked to produce these results. It is also true that the costs in investment, output and productivity growth and in higher levels of unemployment are significant. Post 2007, it has become clear that a Central Bank cannot pursue price stability at all costs.
9. The evidence of asset price bubbles in Nigeria and globally and it is axiomatic that the asset price bubbles are driving the quantitative easing by major Central Banks. As with all speculative bubbles, a bust is inevitable unless forward looking policies are taken to ensure a soft landing. Given the commitment of the Central Banks to quantitative easing through to 2015 and given the scope and size of the bubbles, the scope and size of the "contagion effects" that may result will be significant and the cost for passive countries may be catastrophic.
10. Although, some portfolio flows adjusted downwards in March and April, there is need for further adjustments to levels that would not threaten the financial and economic stability of Nigeria. Human history and Nigeria's recent history provides strong foundation to expect that the flows are reversible while sound theoretical and empirical analysis provides sound foundations in support of a claim that the net flows are non-positive in the medium term.
11. The theory and the evidence anchor two main points. First, future stability of prices, of the exchange rate, of the financial system and of the economy is at risk if volatile financial flows grow unchecked. Second, following from the first, the real choice is between short term stability and, medium to long term stability.

12. In voting for a rate cut therefore, I am voting clearly for medium to long term stability and, for minimizing short to long term costs of instability. I am also voting implicitly for a strengthening of the transmission mechanism of monetary policy, for a forward looking strategy and for institutional changes that limits the depth and scope of the “inverted intermediation” that has become a distinct feature of the Nigerian financial system.

13. Finally, as I have argued before, the tightening phase would have been far more successful at much lower costs also, of a much shorter duration had fiscal policy been substantially more efficient and effective in enhancing the competitiveness of the Nigerian economy through upgrades in infrastructures and in the delivery of sound public services. To reiterate a point the MPC has always made, there is a limit to the set of economic outputs and economic outcomes that monetary policy could deliver without the support of fiscal policy to engineer the necessary structural transformations of the economy. It is important now more than ever that fiscal policy complements monetary policy to deliver price stability, growth and employment given the fragility of the global economy and its susceptibility to volatilities and financial crisis. It is important that government resists the strong domestic/international lobby and, temptation to expand sovereign debt on a ratio or threshold argument which is logically and empirically unsound and totally lacking in wisdom or understanding. The paths of Nigeria in 1978-2006, Greece, Ireland, Portugal, Spain, Italy, Cyprus and, the Euro-zone post 2007 are indicative of what lies ahead if growth in public debt is not aligned to the long term stability of the economy.

4.0 LEMO, TUNDE

Arriving at policy decision at this meeting seems a little bit complex. Current macroeconomic conditions suggest a benign environment, including moderation in inflation with all the measures now in single digit. The foreign reserve level has increased to a fairly comfortable level with demand pressure in the foreign exchange market fairly subdued. In addition, the money market rates have shown good degree of stability while investors' confidence in the economy has increased, evidenced by the declining yields on long term bonds.

The important question, however, is whether the economy has reached a steady state that could allow relaxation of the current tight stance. I am a little bit cautious to affirm this. Although inflation has moderated, the path is less discernible as it has shown fair degree of swings since January 2013, although still in single digit.

It could also be observed that there are some latent underlying inflationary push factors which should be properly managed before the effects fully crystallize. The likelihood of an increase in public expenditure in the remaining quarters of the year may result in the projected fiscal deficit level being exceeded with implication for further government borrowing as well as depletion of excess crude account. On a related note, weakness in the euro area may weigh on external demand for crude oil with implication for crash in the price of crude oil. When this precarious condition is combined with declining oil output at home, the impact would not only be felt on government revenue but also in the foreign exchange market and accretion to reserves. Invariably, widening fiscal deficit and pressure on exchange rate could still stoke inflationary pressure.

The structure of the broad money supply (M2) further revealed the salutary effects of the subsisting tightening stance on inflation environment. Provisional data show that narrow money (M1) declined by 1.90 per cent between end-

December 2012 and end-April 2013 while quasi money grew by 9.86 per cent during the same period or 29.58 per cent on annualized basis. This development, if sustained, implies that a reasonable portion of aggregate money supply would not be immediately available to fuel demand pressure but retained within the banking system to support its stability.

With respect to real output, current level of growth, in the face of various challenges, could be adjudged impressive as the economy recovers from flood related disruptions of 2012. This notwithstanding, the space for monetary policy to stimulate output growth seems diminished as the binding constraints on growth; supply bottlenecks, weak infrastructural condition, and multi-dimensional threats to security have persisted. Except a broad measure of reform that addresses these concerns are urgently put in place, sole reliance on monetary policy as a tool of macroeconomic stabilization may be less effective by the day.

In the light of the above, the monetary policy measures outlined in the March 2013 meeting still remain relevant. In other words, I propose that both the MPR and the CRR be retained at 12 per cent.

5.0 MOGHALU, KINGSLEY CHIEDU

The question before the Monetary Policy Committee is whether the time has come to start easing monetary policy. The answer is that, considering all the circumstances, not yet. It is true that, although headline inflation increased from 8.60 per cent in March 2013 to 9.05 per cent in April 2013, it is still in the single digits, and stable inflation is projected over the next six months. The argument has also been made about the need to reduce rates in order to spur growth.

But there are still some risks in the horizon, and strong arguments for the MPC to

hold rates steady at this time. First, with overall GDP growth for 2013 projected at 6.91 per cent, growth has remained rather robust and thus is not a factor that should outweigh all the other risks that remain the horizon.

Second, the monetary policy stance of the MPC over the past one year has delivered strong results. These include reduced inflation, a stable exchange rate, and real interest rates, in short, price stability overall. If that policy has worked thus far, it may not be helpful to reduce rates prematurely and risk a rise in inflationary trends that have not diminished to an extent that establishes a clear trend and argues for a rate cut. It is important to note that price stability is the primary mandate of the MPC. I have in previous statements addressed the notion that a reduced Monetary Policy rate will bring about increased lending to small and medium enterprises and other parts of the real economy. The evidence of the lending behaviour of banks does not support this position, and I have continued to emphasize the importance of the success of structural economic reforms that are underway before we can see a real behaviour change in the lending profile of banks.

Third, there remains a continuing threat of falling oil revenues, especially as a result of reduced oil output from crude oil theft. This poses a continuing threat to the stability of the exchange rate and the foreign reserves.

Fourth, the security situation in the Northeast region of the country has resulted in the declaration of a state of emergency which, while undoubtedly necessary and appears to have the broad support of opinion across the country, nevertheless has implications for monetary policy that the MPC must factor in. For one, it has led to reported price increases in parts of the country. For another, it may lead to significantly increased spending by the Federal

Government, increasing liquidity pressures. Moreover, there have been significant drawdowns on the excess crude account and further claims on the Federal government since December 2012. Together, these two factors account for about 2 trillion naira, posing a clear continuing liquidity risk.

A consumer expectations survey conducted for the MPC indicates that, while inflation is trending downward from a statistical perspective, inflation expectations remain high. Over 50 per cent of Nigerians surveyed expect price increases in the next 12 months. Asked in a survey whether they would rather have interest rates high and inflation down, over 43 per cent of respondents would rather have rates high and inflation down if faced with a choice, while 16.8 per cent would prefer higher prices with lower rates.

In conclusion, it is welcome that inflation appears to be trending down, precisely because of the tight monetary policy formulated by the MPC. If this is the case, it appears necessary to avoid a reversal of the inflation trends at this time. It would be better to continue to maintain a tight monetary stance at this time in a forward looking manner that factors in the threats indicated above. It is also necessary to maintain real interest rates.

For all these reasons, I vote to maintain the MPR at 12 per cent and all the other monetary aggregates at their present level.

6.0 OSHILAJA, JOHN

I voted that the CBN continues to maintain its current Policy stance, leaving all operating instruments unchanged. The MPC's latest decision means that the CBN's Monetary Policy Rate (MPR) remains unchanged at 12% p.a., with a 2% p.a. symmetry around its Deposit and Lending Rates. The Reserve Requirement

also remains unchanged (i.e. CRR, at 12% flat), as do the Liquidity Ratio (30%), and the Net Open FX Position limit of Nigeria's banks (1%).

Keen observers of recent price trends will pretty much parse available data as we did and note, with relief, the continuing decline in inflation at Headline and Core levels. Current Bank forecasts suggest that these trends can be maintained over the next two quarters at least. At this stage, we could begin arguing that the MPC merits high marks for the role it's playing in promoting macroeconomic stability.

We have gotten our Policy Transmission functions back to normal working condition (with the CBN having broadly stabilized the banking system). We are also maintaining suitable monetary conditions for attracting and nurturing inbound investment flows. This is most directly observable in the relative stability of Naira exchange rates. And, while we freely acknowledge that the composition and structure of these flows should be better, Foreign Portfolio Investment (FPI) flows are helping to rebuild the nation's currency reserve buffers. Furthermore, unlike counterparts in Heavily Indebted Developed Countries (HIDC), Nigerian portfolio investors no longer have to contemplate diverse ways of escaping financial repression. Real rates of return are increasingly available through marketable fixed income securities.

Price stability appears within sight, in addition to which the economy's growth rates are moderating; reflecting continuing weaknesses in the economies of major trading partners – China, the EU, and the US. So why is the MPC, which looks like it's taming inflation, not signaling intentions to begin loosening Policy?

For me, the pressing concern is the emerging possibility of continuing erosions in growth, with steadfast high unemployment, accompanied by rebounds in inflation. In a word, stagflation.

Today's voting pattern reflected two broad issues. First, was the desire – given sub-optimal real sector conditions – to signal continuing awareness and concern about the composition of the Capital Accounts. Especially when viewed against voluntary, but inherently transient, FPI flows as the dominant source of funding. Second, were perceived threats of Fiscal Risks signaled by run-rates in Government spending to date. The rate and character of financing operations raises concerns when viewed against backgrounds of elevated oil export performance and market risks. The majority of members believed the weight of Fiscal Risks be significant enough to warrant further caution; particularly given what appear to be increasingly political dimensions around oil theft.

Upon evaluating aggregate stocks and flows of credit in the economy, we found a striking shift in financing operations of the Federal Government (FGN). For much of 2012, with improved export performance, high oil prices, and its enactment of Fiscal Consolidation measures, the FGN was a net creditor to the economy. Today, we find the FGN becoming a net debtor.

At the end of last year the government had gross credit balances vis-à-vis the economy totaling N 4.1 Trillion. As roughly N 2.8 Trillion of this amount constituted borrowed monies, the Government's net position vis-à-vis the economy, by December 2012, was a net credit balance of N 1.3 Trillion. Fast-forward to the end of last month and we find the gross credit balance falling to N 2.7 Trillion; of which borrowed monies (notably via Treasury bill and bond markets) constituted N 3.5 Trillion. Thus, according to the CBN's provisional calculations for April 2013,

the FGN became “overdrawn” with respect to the economy by approximately N 800 billion; i.e. a net debtor.

From the difference in net credit balances, it is clear that approximately N 2.1 Trillion, or 42% of the Government's roughly N 5.0 Trillion Budget for 2013 has been expended. Is this improved Budget Execution? Or is this accelerating Fiscal Expansion? I am most concerned with the latter because of its likely detrimental impact as surges of fiscally sponsored liquidity. Such developments would upset the somewhat delicate macroeconomic balances the MPC tries to influence. In this event, the CBN would have to vigorously attempt to restore equilibrium, using interest and exchange rates.

It may be argued that there are seasonal patterns to annual government spending; in which case borrowing, to smoothen out uneven but expected cash flows, is reasonable. The FGN's normal expenditure profile may be seasonal in nature but (unless Nigeria now farms oil fields) government revenues are most definitely not. However, the financing of recent flows against prevailing and anticipated economic and political backdrops raises concerns.

The bulk of the funds (N 1.1 Trillion) were drawn from Federation revenue accounts, suggesting that the covered expenditures were recurrent in nature. A further N 0.7 Trillion of new debt was incurred for purposes we presently do not know (covering petroleum subsidies, perhaps), and the balance of N 0.3 trillion may likely have been raised from asset sales or other non-debt sources. Nonetheless, the FGN's revenue trajectory shows clear signs of sliding, while that of its expenditures does not. A continuation of this trend would make the approved Budget more expansionary than it was designed to be. Factor in required further spending to address deepening National Security issues, and then add likely extra-Budgetary spending relating to the upcoming Election

Cycle; which is expected to begin by the end of this year at the earliest. These were calculations I made to arrive at my voting decision.

The latest MPC decision could also be taken constructively, as a desire to not store up problems for the future. I see little value in the Committee encouraging premature notions of a likely easing in Policy, only to have us abruptly reverse course, as events threatened to overtake us. The available evidence on balance suggested that if we started easing today, well before the government spending picture is clarified, we would likely have to reinstate tightening policies sooner, rather than later.

7.0 SALAMI, ADEDOYIN

Though inflation rose slightly, its rate of increase has, for the fourth consecutive month, remained within its 'single digit' target band. Furthermore, Staff forecasts for the rate of price rises over the next six months show Headline inflation continuing to fall – declining from 8.9percent in May, 2013 to 7.2percent in October. Indeed the outlook for inflation provided by Bank staff also shows Core inflation steadily falling from 7percent in May to 6.1percent six months later. Credit continues to grow relatively slowly whilst external reserves have continued to increase – albeit slower than at the same period a year ago.

In addition, aggregate activity growth, at 6.6percent, appears robust even though growth in two key sectors - distribution and Telecoms – slowed relative to the same period last year. Corporate sales performance is perhaps the only 'fly in the ointment'. Compared to what it had been in the first quarter of the preceding year, turnover of 49 NSE-listed firms outside the banking sector, which had published performance, shrank by 3.2percent in Q1 2013. Time perhaps, to commence easing monetary conditions. Finally all the 'ducks are lined up'!

Given the forward looking nature of monetary policy, a more relevant consideration is the nature of threats to the current conditions. In my view, two broad risks cannot be ignored –fiscal challenges arising from oil sector conditions coupled with increasing banking liquidity could bring pressure to bear on the currency with adverse consequences for inflation.

The import of oil sector developments and their implications for fiscal and currency risks continue to cast a shadow over monetary policy especially in relation to inflation management. Even though oil prices have eased, production and export volumes pose a more significant threat to revenues with possible implications for currency risk. According to a recent Reuters report “Nigeria looks set for its lowest crude oil exports in nearly four years in June, shipping lists showed on Tuesday, highlighting how badly theft from pipelines is affecting Africa's largest economy. The lists indicate that Nigeria will export 1.76 million barrels per day (bpd), the lowest level since August 2009, Reuters data showed”. Should this position continue, the adverse implications for the Current Account of the Balance of Payments are clear. The impact of a significant weakening of the Current Account for our currency and thus for inflation management are obvious.

A more immediate concern for the inflation outlook is the changing nature of the relationship between the government and the banking system. In the first 4 months of this year, the Federal Government has transformed from being a net creditor to being a borrower from the banking system. The size of the swing is especially noteworthy – from providing savings of NGN1.353trn in Dec., 2012, the government, by April 2013, had borrowed NGN780bn. A review of its revenue and spending performance in Q1 2013 sheds light on this transformation. Relative to Q1 2012, its actual revenues were 12.6 per cent lower while spending rose by slightly over 15percent.

Available figures continue to show significant liquidity in the banking system. At the end of April, liquidity stood at 70.4percent – higher than 2012 year end of 68percent. By contrast, lending to the private sector has expanded 1.7percent in the same period. Stagnant nongovernment lending by the banks in the face of growing liquidity reiterates the need to urgently find market mechanisms which encourage intermediation in favour of the private sector.

Beyond these, but undoubtedly related to them, is the continuing trend of rising proportion of holdings of Domiciliary Account Deposits in aggregate deposits held by Deposit Money Banks. I track these deposits because, depending on ownership, they just may (and I stress may) provide an indication of the private sector appreciation of risks to the currency. Latest data show this category of deposits have continued to rise and now constitute one-fifth of bank deposits. If these holdings were predominantly government holdings, there may be little to be concerned about. However, with individuals and private companies holding 80percent, it is worth paying attention to developments in that space.

Given the risks on the horizon, I am not convinced that it is appropriate at this time to ease monetary conditions. I thus voted to maintain the current policy parameters.

8.0 UCHE, CHIBUIKE

Since the beginning of this year, I have consistently but unsuccessfully argued that the time has come for MPC to signal an end to its current tight monetary policy stance. The economic trends we have reviewed in this meeting have further strengthened my position on the subject matter. The main essence of our

price stability mandate is to encourage the growth of the real sector of our economy. This remains my overriding concern.

Our current tight monetary policy stance is clearly one of the factors responsible for the high interest rates Nigerian banks charge borrowers. Admittedly reducing MPR alone will not be the sole solution to this problem. We must find creative ways of addressing the issue of the rising spread between deposit and lending rates. It is for instance no exaggeration to conclude that our current policy of relying on moral suasion to attain the above objective has failed. The exploitative and predatory nature of our banking system is further highlighted by the impunity with which some banks defraud the public through fraudulent schemes like the overcharging of interest rates. Thankfully, the CBN has already started to expose such schemes. I however believe that the time has come for us to create a regulatory regime that will provide a strong economic disincentive against such practices.

My above position is no doubt supported by the fact that the health of our real sector is entwined with that of our banking system. The resolution of the banking crisis without growing the real sector is not sustainable in the long run. The need to bring down interest rates is further supported by the recent slowdown in our GDP growth rate. Such a policy move will no doubt ameliorate some of the factors responsible for the slowdown in our economy including the sluggish lending to the real sector. Furthermore, the increasing level of our oil theft is explicit evidence that our current oil rent dependent economy is not sustainable. We must therefore do all in our power to promote economic diversification. Thankfully, we are in a relatively strong position to begin to at least signal a change in direction. The current single digit inflation rate and our relatively strong reserve position are all favorable pointers to this.

In arriving at a decision, I have carefully considered the concerns of my colleagues who argue that our fiscal future is beclouded with uncertainty thus making monetary easing premature at the present time. One such argument is that in the run up to the 2015 elections, politicians must find ways of increasing public expenditures in order to fund the said elections. This could be done directly through the monetization of the excess crude account or indirectly through increased oil thefts, the bloating of oil subsidy expenditures and indiscriminate award of duty waivers. Another argument is that the country is currently at war and that there is likely going to be increased fiscal pressures as a consequence of this.

In my view, the above concerns are exaggerated. I am for instance unable to comprehend the implied assertion that real sector development should be sacrificed because of expected increases in government spending associated with an election that will take place in 18 months' time. This is even more so given the fact that some of the schemes being speculated are clearly fraudulent. Our increased autonomy as a central bank also comes with the increased responsibility to politely but explicitly point out such abuses and their implications in our communiqué. We should never underestimate the corrective pressure such explicit assertions by an autonomous central bank can bring on the fiscal system. Furthermore, I am also not convinced that the state of emergency declared in three states and the issue of excess crude monetization will materially change our fiscal landscape. These are no new terminologies or practices in our recent history. The fiscal policy difference that these policies would cause will therefore be in degree not in kind.

At another level, I am fairly convinced that the current positive noises being made by the leadership of the national assembly with respect to the need for the strict implementation of the approved budget and against extra budgetary

expenditures and fiscal abuses will lead to improved fiscal discipline on the part of Government. It is our duty as a central bank to add fodder to such genuine pressures.

Finally, as I made explicit in the last MPC meeting 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. FDI makes sense only when it is applied to real sector economic development. I therefore believe that the time has come for a rethink of our FDI policies. As a start, we must formulate policies that discourage the inflow of short term FDI. The possible disruptive impact of such a policy would be minimized if this is done in a responsible way.

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

9.0 YAHAYA, SHEHU

The international economic climate is characterised by persisting recession in the Eurozone countries, including France and increasing dark clouds for Germany. The US is showing some signs of recovery in GDP growth, employment and business confidence. The recovery is however, still tentative. China still provides a major impetus for global demand, while India and South East Asia

maintain respectable rates of growth. On the whole therefore, global growth is still anaemic.

Given the weak growth prospects of the global economy, the demand for crude oil is also weakening at a time when there is a rapid expansion in oil and gas production in the US and Canada, and production is due to come on stream in some African countries. The combination of weak demand and increasing supplies in the oil and gas market obviously have important implications for the price of crude oil and for the Nigerian economy.

On the other hand, these developments mean that global prices for manufactured commodities as well as for food are trending downwards in advanced economies, emerging economies and the global economy as a whole.

In Nigeria, GDP growth rate of 6.56% in Q1 of 2013, though a bit lower than the annualized level of growth in Q4 2012, maybe due to seasonal factors, is still robust and is forecast to increase in the next two quarters of 2013.

One of the major challenges facing the Nigerian economy is the prospect of significant declines in oil earnings in the medium term, both due to weakening oil prices and declines in official domestic production occasioned by production disruptions and leakages. Already, this year, actual retained revenue of the federal government has been about 24% lower than budgeted. Yet, there are some concerns that development imperatives and the security situation in the North Eastern part of the country might lead to substantial fiscal deficits, necessitate increased government borrowing and generate inflationary pressures.

On the other hand, the current trend in headline inflation, although showing a slow upward increase to 9.05% year- on- year in April 2013 as compared to 8.6%

in March, is still lower than in February 2013. Headline inflation has been below 10% for the whole of the year so far. Core inflation is lower in April as compared to March, while food inflation has risen to about 10% year-on-year in April, largely driven by imported food inflation. Even more important for monetary policy is that headline inflation is forecast to be under 9% in the next six months.

The Naira exchange rate has been quite stable and is expected to remain so in the near term due to the healthy levels of external reserves and active open market operations by the monetary authorities. Concerns remain however that declines in oil earnings may exert a downward pressure on the external reserves, which may trigger reverse portfolio flows and thereby put some downward pressure on the value of the Naira. These twin pressures may point in the direction of maintaining a tight monetary policy stance. However, should they materialize, it would be necessary for the government to make adjustments in expenditure. The Central Bank would also need to, in that case, be compelled to deploy instruments to mop up excess liquidity and dampen threats to price stability.

Taking all these factors into accounts, we consider the relative weight of the arguments to favour a slight easing of the monetary policy stance with a view to influencing a reduction in lending rates. This will align with initiatives being deployed by the Government and the Central Bank to increase financial access to SMEs, manufacturing and agricultural sectors and thereby strengthen growth, generate jobs and provide a stronger basis for financial and price stability.

We therefore vote to reduce the MPR by 50 basis points and to maintain the CRR at its current level.

10.0 SANUSI, LAMIDO SANUSI, GOVERNOR OF THE CENTRAL BANK OF NIGERIA AND CHAIRMAN OF THE MONETARY POLICY COMMITTEE

The principal discussions leading up to our Monetary Policy Committee Meeting by economists, analysts, the business community and Government revolve around the advocacy in many quarters for monetary easing. Those who make these proposals point out, with good reason, the fact that inflation has remained on target for four consecutive months, the sluggish growth in credit to the private sector and very high intermediation spreads in the credit markets.

The merit in these arguments notwithstanding, I am not convinced that monetary conditions are at the moment too tight, and am also concerned about the outlook in the short – to- medium term. The principal driver of liquidity appears to be Government spending. With the increased rate of monetization of oil revenues and Excess crude savings we have pumped in over N2 trillion through the three tiers of Government. At the level of the Central Government alone, fiscal deficit at end of Q1:2013 was about N235b compared with about N85b in Q1:2012. Also, we have seen a huge reduction in savings and deposits of Central Government and its agencies with the CBN and the Banking System between December and April. All indicators studied suggest that, while the official stance of a commitment to fiscal consolidation remains, the fiscal stance in 2013 is in reality less tight than in 2012.

In addition, there are other factors which increase the risk of even higher spending. There is an on-going military operation in the North-East of the country aimed at bringing to an end the uprising and terrorist attacks of radical groups. The prosecution of the war, and the consequent need to invest in reconstruction and rehabilitation as the country deals with the humanitarian situation, are likely to be costly. Secondly, as we approach 2014 and the nationwide election, political spending is bound to rise. While, to some, it may seem too early to worry about election spending, it is clear to me that

developments such as the Nigerian Governor's Forum Chairmanship fiasco and the forging of alliances among opposition parties are indicative of the earnest commencement of horse-trading and grand-standing among politicians. The process has therefore commenced.

The Global environment does not appear to pose a higher risk now than it did two months ago. The fundamentals of a three-speed global recovery remain, with Europe continuing to make tortuous progress towards resolving its crisis. The principal risk to oil revenues seems to be the theft of oil, production closures and other domestic leakages rather than external developments, even though a gradual decline in oil price is projected into the medium term. The output and revenue shock will have an impact on reserve accretion and add pressure to the exchange rate.

Conclusion

I am of the view that in terms of what we set out to achieve, Monetary Policy has thus far been extremely successful. Principal risks to inflation on a forward looking basis lie in increased Government spending and a weaker currency due to oil revenue shocks. Easing money at this point will add impetus to these inflationary impulses. Indeed, we need to monitor these two risks and be courageous enough to tighten money if they materialize and threaten to undermine stability.

In the light of the above considerations, my vote is to hold.