



**CENTRAL BANK OF NIGERIA**

# **MONETARY POLICY REVIEW**

**August 2012**



**Central Bank of Nigeria**

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## Central Bank of Nigeria

### Mandate

- Ensure monetary and price stability
- Issue legal tender currency in Nigeria
- Promote a sound financial system in Nigeria
- Maintain external reserves to safeguard the international value of the legal tender currency
- Act as banker and provide economic and financial advice to the Federal Government

### Vision

"By 2015, be the model Central Bank delivering Price and Financial System Stability and promoting Sustainable Economic Development"

### Mission Statement

"To be proactive in providing a stable framework for the economic development of Nigeria, through effective, efficient, and transparent implementation of monetary and exchange rate policy, and management of the financial sector"

### Core Values

- Meritocracy
- Leadership
- Learning
- Customer-Focus



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## STATEMENT BY THE GOVERNOR

The main thrust of monetary policy in the first half of 2012 was to contain increased pressure on domestic consumer prices arising from developments within and outside the economy. On the domestic front, the challenges to monetary policy and price stability in the first half of 2012 were the anticipated huge deficit spending plan of the Federal Government and the hike in the price of premium motor spirit (PMS) at a time when inflation inertia was already very strong with headline inflation at end-June 2012 in double digits. External conditions were not favourable either. The debt crisis in Europe had intensified, weakening financial markets, aggregate demand and increasing economic uncertainty. Global energy and food prices trended upward with dire consequences for overall global prices and potentially strong impact on some open economies, including Nigeria.

The environment for monetary policy, therefore, in the first half of 2012 was far from conducive. With the monetary policy stance already tight since October 2011, the scope for the conduct of monetary policy was limited considering the potential impact on yields in the financial markets, cost of liquidity management, financial system stability and the sluggish growth in credit to the private sector. In the circumstance, monetary policy had to be complemented with some administrative and regulatory measures including closer monitoring of the markets and improved communication. Monetary policy had been pushed to the limits and the need for greater fiscal policy engineering became apparent.

In the face of these challenges, greater reliance on proactive liquidity management and the 'leaning against the wind' approach adopted during the period under review proved to be worthwhile in the later months. The Naira exchange rate remained stable within the target band just as short-term (interbank) rates stabilized around the bank's standing lending facility rate in the last couple of months in 2012. With demand pressure in the foreign exchange market abating, the risks of exchange rate instability and significant pass-through of higher global prices to domestic prices were expected to decline in the months ahead.

Overall, the short- to medium-term outlook for the economy suggests that inflationary pressure would moderate particularly as the harvest season sets in, paving the way for more investment and growth. Monetary policy will remain largely proactive and supportive of growth.

**Sanusi Lamido Sanusi, CON**  
Governor,  
Central Bank of Nigeria.





## CHAPTER 1 OVERVIEW

*The primary focus of monetary policy in the first half of 2012 remained the maintenance of price stability*

The primary focus of monetary policy in the first half of 2012 remained the maintenance of price and monetary stability. The Bank continued with tight monetary policy, which commenced in the fourth quarter of 2011. The Bank retained the use of the benchmark interest rate, the Monetary Policy Rate (MPR), signalling the stance of monetary policy and as an anchor for short-term money market and other interest rates in order to rein-in inflation expectations. This was supported by the use of Open Market Operations (OMO); repurchase transactions, standing facilities and Discount Window operations as the major tools of monetary operations to ensure optimal system liquidity. These were complemented with reserve requirements such as cash reserve ratio (CRR) and liquidity ratio (LR). Primary market transactions in government securities and foreign exchange market intervention were also used to support monetary management. The Bank continued to make efforts towards improving communication with market operators and other stakeholders.

In the review period, the MPC held three scheduled meetings during which it maintained the MPR at 12.0 per cent, with a symmetric corridor of +/- 200 basis points around the MPR. The Bank also implemented some administrative and regulatory measures to complement OMO in addressing liquidity concerns and demand pressures in the foreign exchange market e.g. CRR at 8 per cent; LR at 30.0 per cent; and the mid-point of exchange rate at N155/US\$ with a band of +/-3.0 per cent.

Against the background of increased uncertainty in the global economy, the MPC closely monitored developments in the external sector, in the evaluation of policy options in the review period. The slow pace of recovery in the advanced economies, reduced growth momentum in emerging economies, the prolonged financial stress in the euro area and inflationary pressures in the domestic economy were some of the key considerations that defined the monetary policy thrust

of the Bank in the first half of 2012.

The first half of 2012 witnessed relatively slow growth in the monetary aggregates arising mainly from the restrictive stance of monetary policy since the fourth quarter of 2011, more effective management of government liquidity position following the operationalisation of the Treasury Single Account (TSA), increased recourse to bond financing of the fiscal deficit and substantial OMO sales.

Growth in broad money (M2) stood at 1.35 per cent as at end-June 2012, annualised to 2.70 per cent, which was significantly lower than 15.43 per cent as at end-December 2011. This development reflected the contraction in net domestic asset particularly, credit to government, which declined substantially in the review period relative to December and the corresponding period of 2011.

Inflationary pressures remained elevated during the review period owing to a number of factors, including rising global food and energy prices, effects of the partial removal of subsidy on premium motor spirit (PMS) in January 2012, fiscal operations of the Federal Government and the upward review of electricity tariff. Headline inflation (year-on-year) stood at 12.9 per cent at end-June 2012, 2.6 percentage points higher than the 10.3 per cent at end-December 2011. Core and food inflation (year-on-year) stood at 15.2 and 12.0 per cent, respectively, compared with 10.8 and 11.0 per cent at end-December 2011. Nonetheless, the relatively stable naira exchange rate, the lower-than-programme expansion in the monetary aggregates and the tight monetary policy stance had moderating effects on consumer prices during the period.

With the progress achieved in resolving the banking system crisis of 2011, the domestic financial markets stabilized to play key roles in the transmission of monetary policy impulses to the real economy. Thus, improved banking system stability helped to promote the effectiveness of monetary policy. As a direct consequence, short-term interest rates tracked the upper band of the MPR corridor. With the standing lending facility at 14.0 per cent (MPR+200 basis points), interbank interest rates

*The first half of 2012 witnessed relatively slow growth in the monetary aggregates due mainly to the restrictive stance of monetary policy*

were relatively less volatile. The average interbank call and open buy back (OBB) rates rose from 13.88 and 13.57 per cent at end-December 2011 to 14.98 and 14.69 per cent, respectively, at end-June 2012.

The average prime lending rate moved from 16.75 per cent at end-December 2011 to 17.02 per cent at end-June 2012. The average maximum lending rate also rose from 23.21 per cent in December 2011 to 23.44 per cent in June 2012. The average consolidated deposit rate rose from 3.09 per cent in December 2011 to 3.82 per cent in June 2012; thus narrowing the spread between the maximum lending and consolidated deposit rates from 20.12 to 19.62 per cent. The upward movement in rates reflected the tight stance of monetary policy.

*Demand pressure moderated considerably at the wholesale Dutch Auction System (wDAS) segment... exchange rate appreciated at the wDAS and BDC's segments, while it depreciated at the interbank segment...*

Demand pressure moderated considerably at the wholesale Dutch Auction System (wDAS) segment of the foreign exchange market. The exchange rate appreciated at the wDAS and Bureau de Change (BDC) segments, while it depreciated at the interbank window. During the first half of 2012, FGN bonds and NTB auctions were oversubscribed due to attractive yields on the instruments and the increased appetite of local and foreign investors in the Nigerian government-issued fixed income securities.

Real sector performance, though still robust, slightly declined in the review period as data from the National Bureau of Statistics (NBS) indicated that GDP growth rate slowed from 7.68 per cent in Q4 2011 to 6.37 per cent in the first half 2012. The decline in GDP growth rate was attributable to the loss of N207.41 billion in national output during the oil subsidy strike by labour unions in January 2012 and security challenges in most parts of the country.



## CHAPTER 2

### DOMESTIC PRICE DEVELOPMENTS AND THE REAL ECONOMY

*Inflationary pressures persisted owing mainly to domestic output contraction, effects of the partial removal of the subsidy on PMS and increases in electricity tariff*

In the first half of 2012, inflationary pressures persisted owing mainly to domestic output contraction, effects of the partial removal of subsidy on premium motor spirit (PMS) and higher electricity tariff. Other factors that contributed to the domestic consumer price pressures were ratchet effect of fiscal operations, new tariff regimes on imported food items (including rice and wheat) and seasonality effects.

#### 2.1 Domestic Economic Activity

Domestic output growth remained resilient despite severe weaknesses in the global economy. Growth in real Gross Domestic Product (GDP) was 6.38 per cent in the first half of 2012 compared with 7.61 per cent in the corresponding period of 2011. The NBS projects overall real GDP growth rate at 6.85 per cent for fiscal 2012, down from 7.45 per cent in 2011. The NBS estimated that the country lost about N207.41 billion of national output to the week-long nationwide strike action by labour unions that occurred in January 2012, in response to the partial removal of subsidy on PMS.

The non-oil sector remained the major driver of growth, growing by 6.58 per cent in the first half of 2012 with agriculture and services contributing 1.56 and 2.82 percentage points, respectively, compared with 2.70 and 2.79 percentage points in the second half of 2011. The slowdown in the contribution of agriculture to output growth was attributable to flood and security challenges, which affected farming activities in some parts of the country during the review period.

The index of industrial production at 136.3 (1990=100) in the second quarter of 2012, rose by 1.40 per cent from 134.58 in the first quarter of 2012 and by 5.98 per cent compared with the corresponding period of 2011. The development was attributed largely to improved performance of the electricity and manufacturing sub-sectors. The index of manufacturing production, estimated at 106.1 (1990=100) in the second

quarter of 2012, rose by 0.41 and 7.28 per cent over the levels in the first quarter of 2012 and the corresponding quarter of 2011, respectively. Estimated manufacturing capacity utilization also rose marginally by 1.1 percentage points to 57.0 per cent relative to the level in the second quarter of 2011. Similarly, the index of mining production at 146.7 (1990=100) increased marginally by 0.53 and 4.34 percentage points over the levels in the preceding half and the corresponding period of 2011 respectively. The rise was accounted for by the increase in crude oil and gas production.

Global economic recovery remained weak, as reflected in increased downside risks to overall growth in 2012. Key sources of growth vulnerabilities were: the lingering sovereign debt crisis and financial sector fragilities in the Euro zone, the recession in most of Europe; and reduced growth in the US; which continued to affect the export-driven economies of China, India and Brazil. This necessitated a downward review of the projected global output growth for 2012 by the International Monetary Fund (IMF) to 3.5 per cent from 3.9 per cent in July 2012. In particular, growth in the advanced economies was estimated to decelerate from 1.6 per cent in 2011 to 1.4 per cent in 2012.

## 2.2 Trends in Inflation during the First Half of 2012

*Headline inflation trended upwards in the first half of 2012*

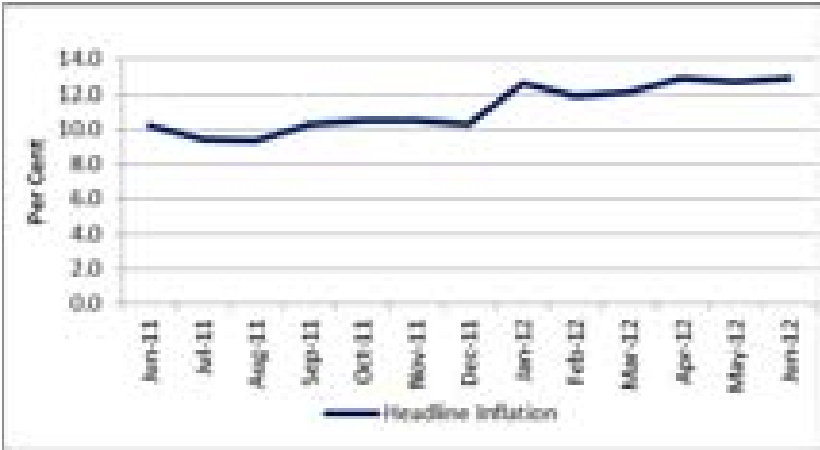
Consumer prices trended upwards in the first half of 2012, driven partly by higher prices of petroleum products, higher electricity tariffs, and increased prices of some farm produce, among others. Inflationary pressures were also fuelled by the below-the-trend performance in agricultural output, traceable to security challenges in some parts of the country.

Headline inflation (year-on-year) fluctuated in the first half of 2012 and stood at 12.9 per cent by end-June, compared with 10.2 and 10.3 per cent at end-June and end-December 2011, respectively.

Food inflation (year-on-year) stood at 12.0 per cent by end-June 2012, compared with 9.2 and 11.0 per cent at end-June and end-December 2011, respectively. Core inflation (year-on-year) stood at 15.2 per cent by end-June 2012, compared with

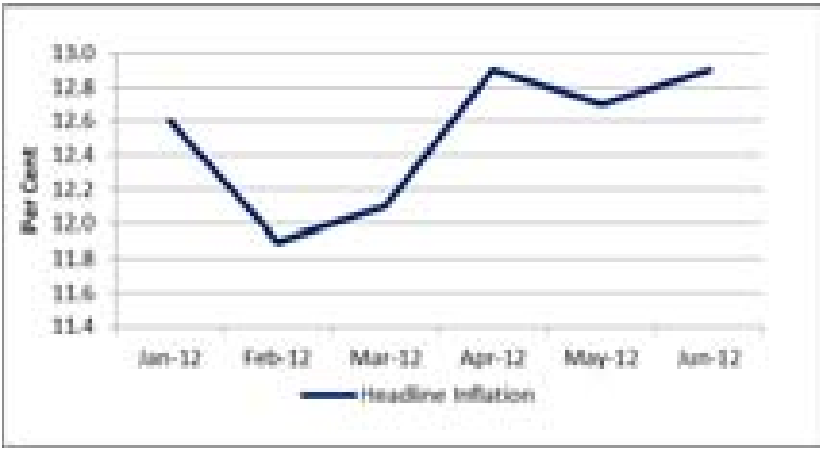
11.5 and 10.8 per cent at end-June and end-December 2011, respectively.

**Figure 2.1**  
**Headline Inflation (June 2011 – June 2012)**



Source: NBS

**Figure 2.2**  
**Headline Inflation (January - June 2012)**



Source: NBS

**Table 2.1**  
**Inflation Rate (June 2011 – June 2012)**

Date	Headline Inflation			Core Inflation			Food Inflation		
	CPI	Y-on-Y	12-MMA	CPI	Y-on-Y	12-MMA	CPI	Y-on-Y	12-MMA
Jun-11	119.90	10.20	12.30	119.80	11.50	12.10	120.10	9.20	12.70
Jul-11	120.30	9.40	12.00	120.10	11.50	12.10	120.40	7.90	12.10
Aug-11	122.30	9.30	11.60	121.20	10.90	12.00	123.70	8.70	11.60
Sep-11	124.00	10.30	11.40	123.50	11.60	11.90	124.80	9.50	11.20
Oct-11	124.60	10.50	11.10	124.80	11.50	11.70	125.00	9.70	10.80
Nov-11	124.70	10.50	11.00	124.60	11.50	11.70	125.40	9.60	10.40
Dec-11	126.00	10.30	10.80	124.80	10.80	11.70	128.10	11.00	10.30
Jan-12	130.20	12.60	10.90	129.10	12.70	11.80	129.30	13.10	10.50
Feb-12	130.50	11.90	11.00	129.30	11.90	11.90	129.10	9.70	10.30
Mar-12	132.60	12.10	10.90	135.10	15.00	12.10	132.10	11.80	10.30
Apr-12	132.80	12.90	11.10	135.20	14.70	12.20	132.30	11.20	10.30
May-12	133.80	12.70	11.10	136.70	14.90	12.40	133.90	12.90	10.40
Jun-12	135.30	12.90	11.30	138.00	15.20	12.70	134.50	12.00	10.60

Source: National Bureau of Statistics (NBS)

**Table 2.2**  
**Quarterly Consumer Price Development (November 2009=100)**

	Sep-11		Dec-11		Mar-12		Jun-12	
	Y-on-Y	12-MMA	Y-on-Y	12-MMA	Y-on-Y	12-MMA	Y-on-Y	12-MMA
Headline %	10.30	11.40	10.30	10.80	12.10	10.90	12.90	11.30
Core %	11.60	11.90	10.80	11.70	15.00	12.10	15.20	12.70
Food %	9.50	11.20	11.00	10.30	11.80	10.30	12.00	10.60

Source: National Bureau of Statistics (NBS)

In the period under review, both core and food components of the consumer price index increased from 124.8 and 128.0, at end- December 2011 to 138.0 and 134.5, respectively. The core index increased by 13.2 points, while the food index rose by 6.5 points. In effect, the core components of inflation exerted greater pressure on headline inflation.



**Figure 2.3**  
**Headline, Core and Food Inflation Rate (June 2011 - June 2012)**



Source: NBS

The contributions of processed food; fruits; and yams, potatoes and other tubers to food inflation decreased from 6.3, 0.6 and 2.0 per cent in January to 4.2, 0.4 and 1.8 per cent in June 2012, respectively. On the other hand, the contribution of meat to food inflation increased from 1.3 per cent in January to 1.4 per cent in June, 2012 (Table 2.3).

**Table 2.3**  
**Selected CPI Components' Contribution to**  
**Food Inflation (Year-on-Year) January – June 2012**

Date	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12
<b>Food %</b>	13.10	9.70	11.80	11.20	12.90	12.00
<b>Processed Food %</b>	6.3	6.0	4.9	3.7	4.5	4.2
<b>Meat %</b>	1.3	0.9	1.4	1.4	1.4	1.4
<b>Fruits %</b>	0.6	0.4	0.4	0.4	0.5	0.4
<b>Yams, Potatoes &amp; Other Tuber %</b>	2.0	1.4	1.8	1.7	1.9	1.8

Source: NBS

Further analysis of the CPI components showed that housing, water, electricity, gas & other fuels; and transport contribution to core inflation in the first half of 2012, declined from 5.3 and

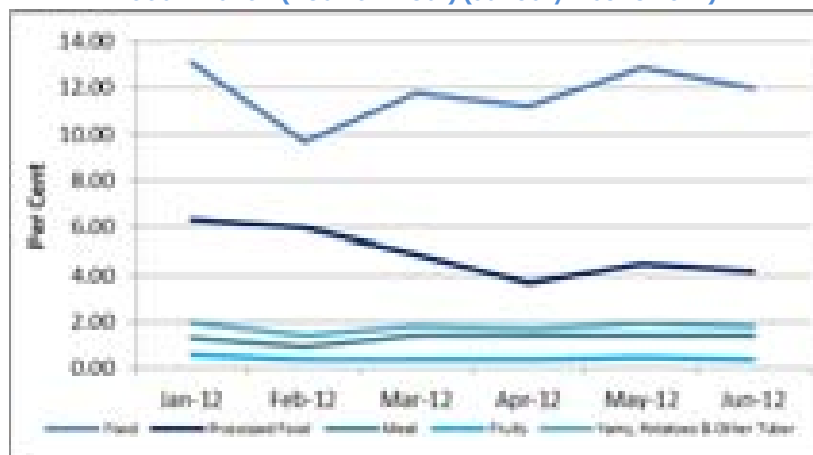
2.2 per cent in January to 4.7 and 1.2 per cent, respectively. Furnishings, household (HH) equipment & HH maintenance; and education increased from 0.8 and 0.3 per cent in January, to 0.9 and 0.7 per cent, respectively, in June 2012 (Table 2.4).

**Table 2.4**  
**Selected CPI Components' Contribution to**  
**Core Inflation (Year-on-Year) (January – June 2012)**

Date	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12
Core %	12.70	11.90	15.00	14.70	14.90	15.20
Housing, Water, Electricity, Gas & Other fuels %	5.3	5.1	6.5	2.6	3.1	4.7
Transport	2.2	1.4	2.0	1.7	1.5	1.2
Furnishings, Household Equip. & HH Maint. %	0.8	0.7	1.2	0.7	1.2	0.9
Education %	0.3	0.3	1.0	1.2	0.8	0.7

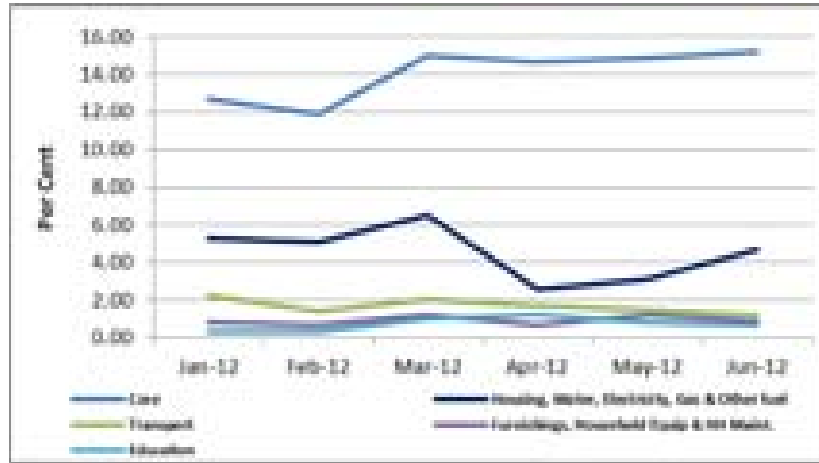
Source: NBS

**Figure 2.4**  
**Selected CPI Components' Contribution to**  
**Food Inflation (Year-on-Year) (January – June 2012)**



Source: NBS

**Figure 2.5**  
**Selected CPI Components' Contribution to**  
**Core Inflation (Year-on-Year) (January – June 2012)**



Source: NBS

**2.3 Actual and Seasonally Adjusted Headline Inflation**

Actual inflation remained higher (except in March 2012) than the seasonally adjusted inflation; indicating influences of seasonality. In the first half of 2012, the most active seasonal factor was the commencement of the planting season when scarcity of food items exerts upward pressure on prices.

**Figure 2.6**  
**Actual and Seasonally Adjusted Headline Inflation**  
**(December 2011 – June 2012)**



Source: NBS

## **2.4 Key Factors that Influenced the Domestic Price Level**

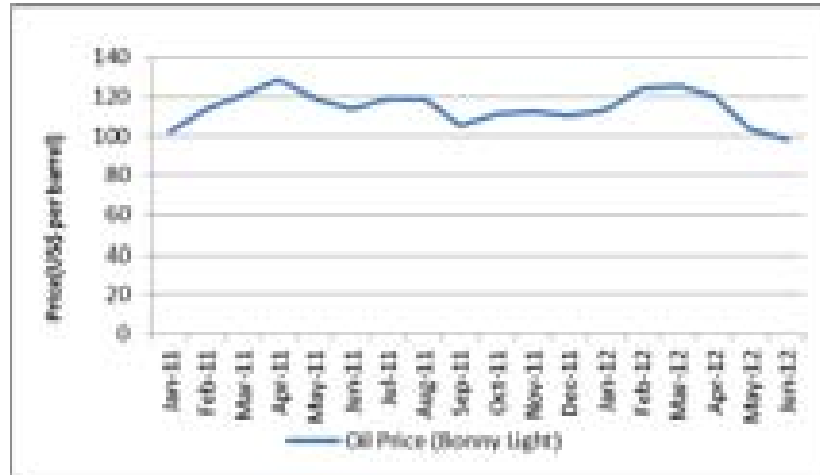
In the first half of 2012, the major factors that influenced inflation in Nigeria were categorized into demand-pull and cost-push factors. There were also some factors which tended to mitigate inflationary pressures in the period under review.

### **2.4.1 Pull and Push Factors**

Government fiscal operations both at the state and federal levels exerted significant pressure on domestic prices in the first half of 2012. The fiscal operations of the Federal Government resulted in substantial increases in domestic liquidity with attendant inflationary risks. Actual fiscal operations of the Federal Government between January and June 2012, resulted in a national budget deficit of N277.92 billion, financed mainly through issuance of bonds. Total Federal Government expenditure during the period amounted to N1,859.58 billion of which N1,133.65 billion or 60.96 per cent was recurrent non-debt expenditure.

Oil prices remained high during the review period (i.e., the prices exceeded the budget benchmark price of US\$72.00 per barrel). By March 2012, the price of Bonny Light crude rose to US\$128.00 per barrel, compared with the level of US\$111.46 per barrel recorded in December 2011, and the average price of US\$113.51 per barrel in the first half of 2011. By June 2012, the price of Bonny Light crude stood at US\$98.06 per barrel. The high oil prices boosted overall federation revenues and supported higher levels of public expenditure across the tiers of government.

**Figure 2.7**  
**Oil Price (Bonny Light) (January – June 2012)**



Source: NBS

Displacement of farmers in some parts of the country due to flood and insecurity accounted substantially for the drop in agricultural output in the review period. The decline in agricultural output and recent security challenges hampered effective distribution of agricultural products, thereby, accentuating higher food prices.

The partial withdrawal of subsidy on PMS in January 2012 was a key driver of inflation through its primary effect on energy and transport costs and secondary effects on other prices. As a result, core inflation rose from 12.7 per cent in January to 15.0, 14.9, and 15.2 per cent in March, May and June, respectively. Imported food prices which had declined to 5.7 per cent in February 2012 rose to 9.9 and 18.5 per cent in May and June 2012, respectively. The escalation in imported food prices was attributed to rising global food inflation due to food shortages. Anticipatory effects of new fiscal measures including the upward review of tariffs on electricity, imported rice and wheat aimed at ensuring an appropriate pricing regime to attract investment into the subsectors further increased pressure on domestic prices. New import tariffs on rice and wheat were announced in the 2012 budget to be implemented from July 1, 2012.

### 2.4.2 Moderating Factors

In the first half of 2012, the CBN maintained the tight monetary policy stance that commenced in 2011, in order to control excess liquidity and rein-in inflation expectations. The MPR and CRR were left unchanged at 12.0 and 8.0 per cent, respectively. Tight monetary policy combined with aggressive liquidity mop-up operations slowed down the growth in the monetary aggregates with a dampening effect on inflation.

Exchange rate management sought to discourage speculative demand for foreign exchange in order to stabilize the naira. Some of the measures taken to keep the naira exchange rate stable were: intervention in the foreign exchange market; and buildup of the stock of external reserves to sustain future demand for foreign exchange. In the first half of 2012, the stock of external reserves rose by 12.50 per cent from US\$32.64 billion at end-December 2011 to US\$36.72 billion. On account of these developments, the naira appreciated against the dollar during the period, thus moderating inflation expectations. The naira opened at N158.27/US\$ at end-December 2011 and closed at N157.50/US\$ on 30<sup>th</sup> June 2012, indicating an average exchange rate of N157.62/US\$, and appreciation of N0.77 or 0.49 per cent. Similarly, at the Bureau de Change (BDC) segment, the exchange rate opened at N166.00/US\$ and closed at N164.00/US\$ with an average exchange rate of N161.13/US\$, indicating an appreciation of N2.00 or 1.20 per cent.

The slow growth in the monetary aggregates had a dampening effect on domestic prices. Broad money supply (M2) grew marginally by 0.01, 2.25 and 1.35 per cent, or at annualized rates of 0.03, 5.40, and 2.70 per cent, in April, May, and June 2012, respectively, compared with 15.40 per cent at end-December 2011. Aggregate domestic credit (net) declined by 3.18, and 2.73 per cent, in May and June 2012, respectively, relative to the level at end-December 2011.

**Box 2.1****Implementation of Treasury Single Account and Price Stability in Nigeria**

Imperfect information on government finances is a common phenomenon in many emerging and developing countries due to the fragmented nature of public sector banking arrangements. This results in Ministries, Departments and Agencies (MDAs) operating multiple bank accounts; which impede effective cash management and control. To address this concern, the Federal Ministry of Finance (FMF) and the Office of the Accountant-General of the Federation (OAGF) in collaboration with the Central Bank of Nigeria, with technical support from the World Bank and the International Monetary Fund (IMF) introduced the Treasury Single Account (TSA) initiative on a pilot scheme in the first half of 2012. The TSA is aimed at overcoming the problems associated with multiplicity of accounts and idle balances to improve government cash management and control processes. It is a unified system that consolidates government cash balances, improves cash flow and reinforces budget controls and monitoring. In view of the aforementioned benefits, this system enjoys widespread adoption by several countries especially as it conforms with best practice.

**TSA implementation in Nigeria**

The TSA implementation is in four phases. The first phase, which commenced in August 2011, involved linkage of the Consolidated Revenue Fund (CRF) Account of the Federal Government with MDAs capital account balances. The second phase which commenced in January 2012 was to consolidate balances of the CRF including moving MDAs balances from DMBs to the Federal Government single account (CRF) or connected accounts in the CBN. The Government Integrated Financial Management Information System (GIFMIS) is expected to take off in the 3rd – 4th quarters of 2012 to support the planned TSA banking arrangement by which time all the transitional accounts would be closed and their balances transferred to TSA. Linkage of Donor funds and Government controlled trust/social security funds to TSA/CRF account would be made in 2015. Upon full implementation, TSA is expected to achieve unification of all bank accounts of MDAs, eliminate floats in the system, and allow the Treasury comprehensive overview and coverage of all sources of revenue to the Federal Government on real time basis.

**Implications for Monetary Policy**

The domiciliation in CBN of all MDA funds would reduce banking system liquidity and the cost of Open Market Operations. Also, the reduction of government idle funds with DMBs would reduce speculative pressures on the naira exchange rate. TSA would reduce the Federal Government's utilization of Ways and Means Advances which involves creation of high-powered money which is inimical to the price stability objective of the Bank. Thus, cash management and monetary policy would be more effective when the cash balance targeting model of TSA system is fully implemented.





## CHAPTER 3 MONETARY POLICY

*The Bank maintained a tight monetary policy stance in the period, in order to mitigate inflationary pressures arising from the partial removal of subsidy on PMS*

The thrust of monetary policy in the first half of 2012 remained the achievement of price stability conducive to economic growth. The Bank maintained a tight monetary policy stance in the period, in order to mitigate inflationary pressures arising from the partial removal of subsidy on PMS and other fiscal policy measures (upward adjustment of tariffs on electricity and imported rice/wheat). The Monetary Policy Committee (MPC) held three scheduled meetings during the first half of 2012 and left the MPR unchanged at 12.0 per cent.

*The MPR was unchanged at 12.0 per cent in the three meetings held in the first half of 2012*

### 3.1 Highlight of Monetary Policy Measures

In the period under review, the Bank maintained its restrictive stance on monetary policy. The MPR was unchanged at 12.0 per cent in the three meetings held in the first half of 2012. In addition, the CRR was maintained at 8.0 per cent. Similarly, the foreign exchange net open position of banks remained at 3.0 per cent in the review period. Besides the retention of MPR and CRR, the mid-point of the exchange rate remained at N155.00/US\$1.00 with the band of +/- 3.0 per cent, in order to sustain the stability of the domestic currency and build-up external reserves as well as provide conditions that were conducive to the inflow of foreign investment.

Key considerations that informed the retention of tight monetary policy by the Bank included the partial removal of the subsidy on PMS in January 2012; the announcement effect of the planned increases in import tariff on rice and wheat effective from July 2012; and in electricity tariff effective from June 2012. Also, the Committee recognized the limitations of monetary policy with respect to inducing long-term growth and that it must be complemented by fiscal and structural policies relating to petroleum and infrastructure sectors.

### 3.2 Monetary Policy Committee (MPC) Decisions

The MPC at its January 2012 meeting underscored the need for price stability conducive to economic growth. In this regard, it observed that the announced increase in import tariff on some food items would exert further pressure on food prices which

could compound the effect of increased transportation costs induced by the partial removal of fuel subsidy. The Committee noted that historically, upward adjustments in the price of PMS had tended to have a short-term impact on the rate of inflation. A review of previous instances of adjustments in fuel prices showed that without exception, each instance was accompanied by an increase in the rate of inflation followed almost immediately by a moderation in the short- to - medium term. Considering the impact of previous tightening on inflation and the naira exchange rate up to December 2011, the Committee unanimously agreed to retain the policy rate (MPR) at 12.00 per cent, along with the symmetric interest rate corridor of +/-200 basis points around the MPR.

*...the Committee noted that the prevailing inflationary pressure from supply shocks would have been more severe if there had been no mitigating factors on the demand side*

At the meeting of March 2012, the Committee noted that the prevailing inflationary pressures from supply shocks would have been more severe if there had been no mitigating factors on the demand side. The Committee observed that aggregate credit and broad money (M2) had been on the decline and there were signs of improving fiscal position with some control over expenditure and no imminent increase in wages. The fiscal stance and the absence of second-round effects of the fuel subsidy removal had complemented the monetary policy stance to dampen demand. The situation was further supported by the stable exchange rate and improved international commodity prices which combined to moderate imported inflation. However, there was no incentive to reduce the policy rate because inflationary threats re-emerged in March 2012 after moderating in February. In particular, food and core inflation rose sharply during the month of March 2012 to 11.8 and 15.0 per cent respectively, compared with 9.7 and 12.7 per cent in February. In the light of these developments, and considering the beneficial effects of previous tightening on inflation and the exchange rate up to February 2012, the Committee unanimously decided to retain the benchmark rate (MPR) at 12.00 per cent and the corridor at +/- 200 basis points.

At the MPC meeting of May 2012, the Committee noted that the uncertainty surrounding the global economy remained

elevated owing to continued economic slowdown in advanced and major emerging economies as well as the financial stress in the Euro zone. These developments were likely to impact the domestic economy through trade and financial channels, thereby weakening the external and fiscal positions. Furthermore, the Committee reviewed the output data which indicated a slowdown in GDP growth. It noted that the huge drop in agricultural output was traced to the following factors: displacement of farmers in the northern part of the country owing to insecurity, inadequate rainfall and increased production costs due to the partial removal of fuel subsidy in January 2012. The Committee concluded that a downward adjustment in the policy rate would not be effective in stimulating growth under the prevailing circumstance. It was the Committee's view that the sluggish growth in credit, stable exchange rate, healthy external reserve position and benign month-on-month inflation did not suggest a need for further tightening. However, in rejecting the alternative proposal for policy rate reduction, the MPC reasoned that the causes of the slowdown in agriculture and oil GDP growth would not be addressed by monetary easing alone. Consequently, the Committee unanimously voted to maintain the restrictive stance of monetary policy. Consequently, the MPR was retained at 12.0 per cent, along with the symmetric band of +/- 200 basis points around the MPR. The CRR and Liquidity Ratio (LR) were also left unchanged.

**Table 3.1**  
**MPC Decisions (January – June, 2012)**

Items	January	March	May
<b>MPR</b>	Retained the MPR at 12.00%	No Change	No Change
<b>MPR Corridor</b>	Retained the corridor at +/- 200 basis points	No Change	No Change
<b>SDF Rate</b>	Retained at 10.00%	No Change	No Change
<b>SLF Rate</b>	Retained at 14.00%	No Change	No Change
<b>CRR</b>	Retained at 8.00%	No Change	No Change
<b>LR</b>	Retained at 30.00%	No Change	No Change
<b>NOP</b>	Retained at 3.00%	No Change	No Change
<b>FX Rate Mid-Point</b>	Retained at N155.00/US\$1.00	No Change	No Change
<b>FX Band</b>	Retained at +/- 3.00%	No Change	No Change

### 3.3 Monetary Policy Instruments

The overriding consideration of the MPC during the review period was to maintain price and exchange rate stability, build-up external reserves, and create a conducive environment for attracting and retaining foreign investment. In choosing the instruments to realize these objectives, the MPC was guided by the need for consistency and stability in the domestic macroeconomic environment.

#### 3.3.1 Monetary Policy Rate (MPR)

The MPR, the Bank's benchmark policy rate, remained the major signalling instrument complemented by the standing (lending/deposit) facilities. The Committee kept the MPR unchanged at 12.0 per cent during the three meetings held in the review period. This decision maintained the restrictive stance of monetary policy to keep inflation in check.

### 3.3.2 Reserve Requirements

The Bank retained the use of reserve requirements: cash reserve ratio (CRR) and liquidity ratio (LR) in the period to complement OMO and other instruments of liquidity management. The CRR was retained at 8.0 per cent while the LR was unchanged at 30.0 per cent in the first half of 2012.

*...subscription was N5,051.93 billion... Actual sales, however, amounted to N1,717.35 billion in the first half of 2012, compared with N1,582.02 billion in the second half of 2011*

### 3.3.3 Open Market Operations (OMO)

The Bank continued the use of OMO as the major tool of liquidity and monetary management. The CBN Bills were the main securities for OMO operations during the period. Total amount on offer was N2,760.00 billion, while subscription was N5,051.93 billion. Actual sales, however, amounted to N1,717.35 billion in the first half of 2012, compared with N1,582.02 billion in the second half of 2011 and N1,466.48 billion in the corresponding period of 2011, representing an increase of 8.6 and 17.1 per cent, respectively.

**Table 3.2**  
**CBN OMO Bills Auction (N'million) January 2009 – June, 2012**

Date	2009	2010	2011	2012	% Change over the Preceding Year
Jan	115.47	149.83	205.59	246.64	
Feb	80.11	100.22	216.92	297.70	
Mar	80.00	65.00	284.06	491.59	
Apr	101.36	160.49	215.07	304.18	
May	120.22	100.22	204.60	363.13	
Jun	120.00	158.70	340.24	14.12	
<b>1st Half</b>	<b>617.16</b>	<b>734.46</b>	<b>1,466.48</b>	<b>1,717.35</b>	<b>8.6</b>
Jul	125.36	250.91	209.74		
Aug	105.22	141.16	218.92		
Sep	91.76	206.57	280.57		
Oct	170.26	167.01	309.95		
Nov	120.22	205.93	242.93		
Dec	162.56	297.91	319.91		
<b>2nd Half</b>	<b>775.38</b>	<b>1,269.49</b>	<b>1,582.02</b>		
<b>Cumulative Figure</b>	<b>1,392.54</b>	<b>2,003.95</b>	<b>3,048.50</b>		

*The Bank's standing facilities (lending/deposit) were available to DMBs to meet their daily liquidity needs*

### 3.4 Standing Facilities

The Bank's standing facilities (lending/deposit) were available to DMBs to meet their daily liquidity needs. In the first half of 2012, both facilities were actively used by the DMBs and discount houses. The cumulative volume of transactions at the CBN standing lending facility (SLF) in the first half of 2012 stood at N10,721.44 billion compared with N25,047.27 billion in the second half of 2011 and N17,628.64 billion in the corresponding period of 2011. The cumulative volume of SLF at end-June 2012 represented a decrease of 57.19 and 39.18 per cent compared with the level in the second half of 2011 and the corresponding period of 2011, respectively (Table 3.3). This development was a reflection of improved liquidity conditions driven principally by AMCON injections, huge repayments of matured FGN bonds and CBN securities.

**Table 3.3**  
**CBN Standing Lending Facility (N'billion)**  
**(January 2009- June 2012)**

Date	2009	2010	2011	2012	Percentage change over the preceding/corresponding period
Jan	846.18	135.50	565.51	939.16	
Feb	3,457.57	-	1,369.60	1,060.90	12.96
Mar	4,592.69	-	3,425.47	2,053.62	93.57
Apr	3,875.48	-	3,328.35	1,875.31	(8.68)
May	2,581.43	270.97	3,722.41	1,472.21	(21.50)
Jun	3,691.75	21.70	5,217.30	3,320.24	125.53
<b>1st Half</b>	<b>19,045.11</b>	<b>428.17</b>	<b>17,628.64</b>	<b>10,721.44</b>	<b>(39.18)</b>
Jul	4,675.02	55.76	3,334.91		
Aug	3,733.78	0.00	2,714.70		
Sep	2,287.90	73.10	7,698.83		
Oct	1,231.61	983.44	6,675.79		
Nov	537.58	1,374.80	2,592.94		
Dec	1,022.60	853.50	2,057.10		
<b>2nd Half</b>	<b>13,488.49</b>	<b>3,340.60</b>	<b>25,047.27</b>		
<b>Total</b>	<b>32,533.60</b>	<b>3,768.77</b>	<b>42,702.91</b>		

The cumulative volume of transactions at the CBN Standing Deposit Facility (SDF) stood at N3,727.96 billion in the first half of 2012 compared with N1,435.82 billion in the second half of

2011 and N3,132.04 billion in the corresponding period of 2011. The level of SDF as at end-June 2012 represented 159.64 and 19.03 per cent increases over the levels in the second half of 2011 and the corresponding period in 2011, respectively (Table 3.4). The observed increase in the use of the SDF window when compared with the corresponding period of 2011 was due to the non-remuneration under the facility between March and October 2011 when the reserve averaging scheme was in operation.

**Table 3.4**  
**CBN Standing Deposit Facility (N'billion)**  
**(January 2009- June 2012)**

Date	2009	2010	2011	2012	% Change over the preceding period
Jan	-	5,622.63	1,864.84	868.10	
Feb	-	6,101.90	721.62	788.26	(9.20)
Mar	-	9,413.45	325.75	352.85	(55.24)
Apr	-	6,853.06	49.65	201.00	(43.04)
May	-	1,735.45	73.00	1,242.50	518.20
Jun	-	5,563.64	97.18	275.25	(77.85)
<b>1st Half</b>	-	<b>35,290.13</b>	<b>3,132.04</b>	<b>3,727.96</b>	<b>19.03</b>
Jul	162.00	4,055.52	-		
Aug	1,453.38	6,849.71	-		
Sep	1,058.75	4,224.80	-		
Oct	3,106.30	1,117.30	422.50		
Nov	1,050.59	443.78	436.47		
Dec	1,797.92	1,191.78	576.85		
<b>2nd Half</b>	<b>8,628.94</b>	<b>17,882.89</b>	<b>1,435.82</b>		
<b>Cumulative Figure</b>	<b>8,628.94</b>	<b>53,173.02</b>	<b>4,567.86</b>		

*The Bank continued its intervention in the foreign exchange market to sustain the stability of the naira*

### 3.5 Foreign Exchange Intervention

In the first half of 2012, the Bank continued its intervention in the foreign exchange market to sustain the stability of the naira. Total supply of foreign exchange by the Bank in the review period stood at US\$13,861.67 million compared with US\$23,458.70 million and US\$17,002.68 million in the preceding half year and the corresponding period of 2011, respectively (Table 3.5). Total supply in the first half of 2012 decreased by 40.91 and 18.47 per cent from the levels in the second half and

the corresponding period of 2011, respectively. The sharp decline in demand reflected more detailed documentation and monitoring by the Bank to sanitize the foreign exchange market. These measures were complemented by increased autonomous foreign exchange inflows.

**Table 3.5**  
**Foreign Exchange Supply by the CBN (US\$ million)**

YEAR	2010			2011			2012		
	Sales to wDAS	Sales to BDC	Total Supply (wDAS + BDC)	Total wDAS sales	Sales to BDC	Total Supply (Total wDAS + BDC)	Sales to wDAS	Sales to BDC	Total Supply (wDAS + BDAC)
Jan	1,461.75	429.17	1,890.92	2,000.00	135.54	2,135.54	1,640.65	365.73	2,006.38
Feb	1,838.85	279	2,117.85	1,794.85	300.04	2,094.89	1,942.18	720.59	2,662.77
Mar	1,582.02	482.19	2,064.21	3,274.38	330.53	3,604.91	1,452.75	698.16	2,150.91
Apr	1,841.07	306.05	2,147.12	2,385.58	322.26	2,707.84	891.52	492.76	1,384.28
May	2,707.47	277.34	2,984.81	2,825.19	392.03	3,217.22	1,487.00	625.52	2,112.52
Jun	2,283.95	657.49	2,941.44	2,894.96	347.32	3,242.28	3,000.00	544.81	3,544.81
1st Half	<b>11,715.11</b>	<b>2,431.24</b>	<b>14,146.35</b>	<b>15,174.96</b>	<b>1,827.72</b>	<b>17,002.68</b>	<b>10,414.10</b>	<b>3,447.57</b>	<b>13,861.67</b>
Jul	1,835.20	741.16	2,576.36	2,895.51	398.15	3,293.66			
Aug	1,948.52	450.84	2,399.36	3,172.69	504.28	3,676.97			
Sep	3,593.54	613.77	4,207.31	4,161.90	995.65	5,157.55			
Oct	2,342.08	478.71	2,820.79	3,406.03	716.76	4,122.79			
Nov	1,561.68	280.21	1,841.89	3,260.91	795.37	4,056.28			
Dec	<b>1,839.13</b>	<b>341.11</b>	<b>2,180.24</b>	<b>2,475.80</b>	<b>675.65</b>	<b>3,151.45</b>			
2nd Half	<b>13,120.15</b>	<b>2,905.80</b>	<b>16,025.95</b>	<b>19,372.84</b>	<b>4,085.86</b>	<b>23,458.70</b>			
Total	<b>24,835.26</b>	<b>5,337.04</b>	<b>30,172.30</b>	<b>34,547.80</b>	<b>5,913.58</b>	<b>40,461.38</b>			

### 3.6 Performance of Monetary Aggregates

Growth in broad money stock (M2) in the first half of 2012 remained below the 2012 first half indicative target. It grew by N179.87 billion or 1.35 per cent over the end-December 2011 level as against N1, 131.39 billion or 9.29 per cent in the second half of 2011 (Table 3.6). On annualized basis, the growth in broad money was 2.70 per cent, lower than the target of 24.64 per cent. Narrow money (M1) decreased by N171.88 billion or 2.54 per cent in contrast to an increase of N1, 134.32 billion or 20.12 per cent in the second half of 2011. M1 contracted by 5.08 per cent on annualized basis, falling short of the annual growth target of 34.71 per cent by 39.79 percentage points. The weak performance of the monetary aggregates was

*....broad money stock (M2) in the first half of 2012 remained below the 2012 indicative target*

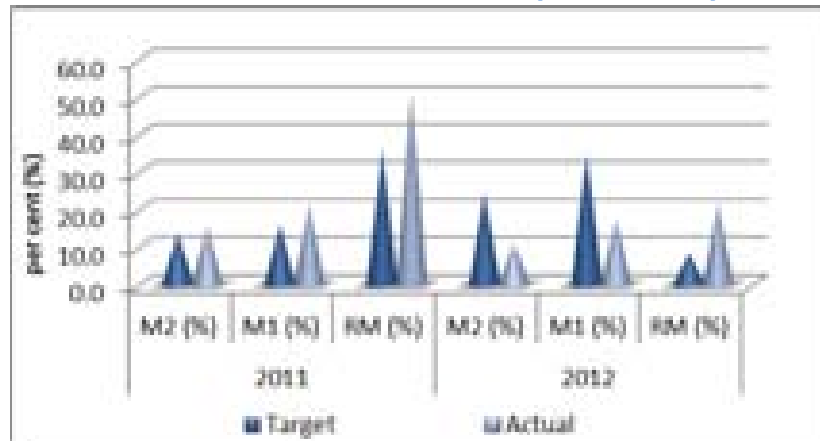


attributed to a more effective management of government liquidity position (following the implementation of the TSA), increased recourse to bond financing of deficit and substantial OMO sales.

**Table 3.6**  
**Performance of Monetary Aggregates**

	2011				2012		Change in 2011:H2	Change in 2012:H1
	Actual June 2011	Target 2011	Actual Dec 2011	Deviation	Target 2012	Actual June 2012	Actual	Actual
<b>M2 (N'b)</b>	12,172.10	12,790.88	13,303.34	-509.46	16,577.53	13,483.36	1,131.39	179.87
<b>M2 (%)</b>	12.23	13.6	15.43	4.42	24.64	10.77	9.29	1.35
<b>M1(N'b)</b>	5,637.26	6,095.31	6,771.58	673.11	9,117.64	6,599.70	1,134.32	-171.88
<b>M1 (%)</b>	14.63	15.8	21.54	12.08	34.71	17.07	20.12	-2.54
<b>RM (N'b)</b>	2,065.06	2,515.28	2,784.07	268.99	3,013.32	2,512.47	719.01	-271.60
<b>RM (%)</b>	34.52	36.28	54.84	18.06	8.23	21.67	34.82	-9.76
<b>NDC (N'b)</b>	8,889.64	11,715.59	13,686.73	687.58	18,873.49	13,313.08	4797.09	-373.65
<b>NDC (%)</b>	3.21	29.3	57.16	7.9	52.17	49.76	53.96	-2.73
<b>Cg (N'b)</b>	-1,068.31	-974.07	-496.86	-442.91	-204.66	-1,380.53	571.45	-883.67
<b>Cg (%)</b>	28.30	13.17	55.71	39.48	61.47	-29.23	-53.49	177.85
<b>Cp (N'b)</b>	9,957.95	12,689.65	14,183.59	244.69	19,078.15	14,693.61	4,225.64	510.02
<b>Cp (%)</b>	-1.43	29.09	44.28	2.49	47.50	47.56	42.43	3.60
<b>NFA (N'b)</b>	6,453.69	6,940.58	7,138.67	240.05	7,654.56	7,525.21	684.98	386.54
<b>NFA (%)</b>	-0.48	6.67	9.71	3.69	6.60	16.60	10.61	5.41

**Figure 3.1**  
**The Performance of M2, M1 and RM (2011 and 2012)**



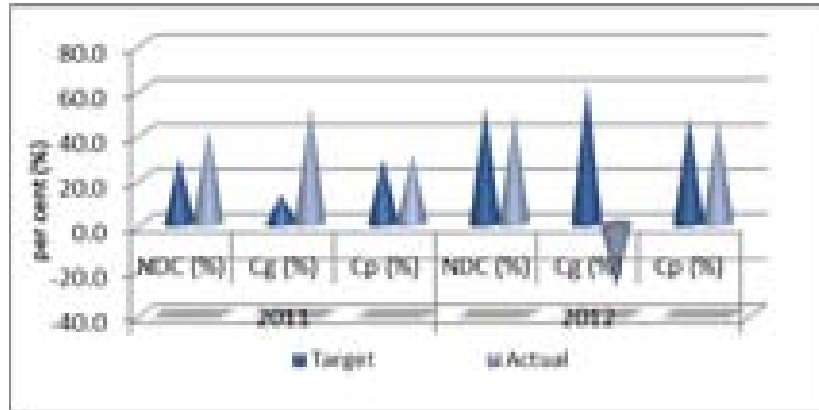
Reserve Money (Base money) decreased in the first half of 2012. It fell by N271.80 billion or 9.76 per cent as against an increase of N719.17 billion or 34.82 per cent in the second half of 2011. Overall, reserve money was N2, 512.47 billion at end-June 2012, which was below the indicative benchmark of N3, 013.32 billion for the year by N500.85 billion or 16.62 per cent.

*Domestic credit decreased by N373.65 billion or 2.73 per cent at end-June 2012 compared with an increase of N4, 797.09 billion....*

Aggregate domestic credit decreased by N373.65 billion or 2.73 per cent at end-June 2012 compared with an increase of N4, 797.09 billion or 53.96 per cent in the second half of 2011. In relation to end-June 2011, aggregate credit grew by 49.76 per cent. Credit to government decreased by N883.67 billion or 177.85 per cent in the first half of 2012 in contrast to an increase of N571.45 billion or 53.49 per cent in the second half of 2011. The sharp decrease was partly attributable to greater reliance of the FGN on public financing (issuance of bonds) and better management of its cash flow under the TSA.

Aggregate credit increased by 5.46 per cent, on annualized basis compared with the target of 52.17 per cent. Credit to government decreased by 177.85 per cent (annualized at 355.70 per cent) compared with the target growth of 61.47 per cent. In effect, the public sector was a net financier to the banking system at the end of the first half of 2012.

**Figure 3.2**  
**The Performance of NDC, Cg and Cp (2011 and 2012)**



*Credit to the private sector increased to N14, 693.61 billion in the first half of 2012 from N14, 183.59 billion at end-December 2011*

Credit to the private sector increased to N14, 693.61 billion in the first half, an increase of N510.02 billion or 3.60 per cent. Compared with the corresponding period of 2011, credit to the private sector increased by N4, 225.64 billion or 42.43 per cent. On annualized basis, credit to private sector grew by 7.20 per cent as against the target of 47.50 per cent.

The Net Foreign Assets (NFA) of the banking system rose by N386.54 billion or 5.41 per cent compared with N684.98 billion or 10.61 per cent in the second half of 2011. On annualized basis, NFA increased by 10.82 per cent compared with the target of 6.60 per cent. The growth in the first half of 2012 was due largely to tight monetary policy, the high price of crude oil in the early part of the year and increased private inflow.



## CHAPTER 4 DOMESTIC FINANCIAL MARKETS

*Money market activities in the first half of 2012 were largely influenced by the relatively high short-term interest rates*

### 4.1 Money Market

Transaction in money market instruments remained active in the first half of 2012, being the main channel for trade in short-term financial assets. Transactions were dominated by Government and CBN securities for OMO; repurchase transactions and Discount Window (DW) operations. Money market activities in the first half of 2012 were largely influenced by the relatively high short-term interest rates. The relatively high money market rates induced the inflow of foreign capital to take advantage of high returns on naira-denominated assets. Money market activities were also influenced by the fiscal operations<sup>1</sup> of the three tiers of government which, though transitory were nonetheless disruptive to the Bank's liquidity management operations.

*Stabilizing short-term interest rates around the policy rate remained a challenge to monetary management... exacerbated by the destabilizing impact of the sharing of revenue...*

#### 4.1.1 Developments in Short-Term Interest Rates

Stabilizing short-term interest rates around the policy rate remained a challenge to monetary management. It was exacerbated by the destabilizing impact of the sharing of revenue proceeds in the Federation Account by the three tiers of government which created system-wide liquidity swings and volatility in short-term interest rates (figure 4.1). The average interbank call rate ranged between 13.35 and 14.98 per cent, while the open buy back (OBB) rate ranged from 10.07 to 14.69 per cent in the first half of 2012.

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<sup>1</sup> Notable among this is the Federation Accounts Allocation Committee disbursements that hold every month. The meeting is held to distribute among the three tiers of government revenue proceeds in the Federation Account based on the revenue allocation formula.

**Table 4.1**  
**Weighted Average Money Market Interest Rates (%)**  
**(December 2011 – June 2012)**

Month	Monetary Policy Rate	Overnight Interest Rates		90-Day Rates	
		Call Rate	Open-Buy-Back	NIBOR	NTB
Dec-11	12.00	13.88	13.57	15.88	14.76
Jan-12	12.00	14.18	13.81	15.25	15.91
Feb-12	12.00	14.29	13.64	15.54	15.14
Mar-12	12.00	14.33	13.90	16.93	15.45
Apr-12	12.00	14.23	13.75	14.96	12.30
May-12	12.00	13.35	10.07	14.54	14.46
Jun-12	12.00	14.98	14.69	16.76	14.54

**Figure 4.1**  
**Weighted Average Money Market Rates (December 2011-June 2012)**

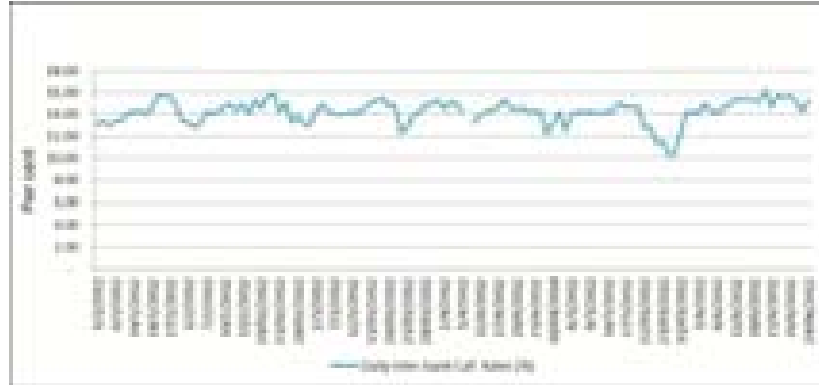


*..weighted average interbank call rate which was 13.88 per cent in December 2011 rose to 14.33 per cent in March 2012 and... to 14.98 per cent in June..*

**(i) Interbank Call Interest Rate**

The weighted average interbank call rate which was 13.88 per cent in December 2011 increased to 14.18 and 14.29 per cent in January and February, 2012, respectively. The rate rose further, from 14.33 per cent in March 2012 to 14.98 per cent in June. Overall, the interbank rate increased by 110 basis points from 13.88 per cent in December 2011 to 14.98 per cent in June 2012. On a year-on-year basis, the weighted average interbank call rate rose by 332 basis points from 11.66 per cent in June 2011 to 14.98 per cent in 2012 (Figure 4.1).

**Figure 4.2**  
Daily Interbank Call Rate (Jan. – June. 2012)



The weighted average OBB rate which was 13.57 per cent in December 2011... peaked at 14.69 per cent in June.

**(ii) Open Buy-Back Rate**

The weighted average OBB rate which was 13.57 per cent in December 2011 rose to 13.81 per cent in January and further to 13.90 per cent in March and peaked at 14.69 per cent in June. Thus, the OBB rate increased by 112 basis points from 13.57 per cent in December 2011 to 14.69 per cent in June 2012. On year-on-year basis, the weighted average OBB rate increased by 5.1 percentage points from 9.59 per cent in June 2011 to 14.69 per cent in June 2012 (Figure 4.1).

**Figure 4.3**  
Daily Open-Buy-Back Rate (Jan. - Jun. 2012)



### iii Nigeria Interbank Offered Rate (NIBOR)

*The weighted average 90-day NIBOR rate which was 15.88 per cent in December 2011.. rose to.. 16.76 in June 2012.*

The NIBOR remained the traditional reference rate for tenored transactions. The 90-day NIBOR rate moved in tandem with the interbank call and OBB interest rates in the first half of 2012. The weighted average 90-day NIBOR rate which was 15.88 per cent in December 2011 moderated to 15.25 per cent in January, then rose to 16.93 and 16.76 per cent in March and June 2012, respectively(Figure 4.1).

The general decline in short-term rates in January was due to liquidity surfeit arising from injections into the system traced to the delayed payment of December statutory revenue in January and the revaluation of the AMCON bonds. The effect of the injections lasted through February, thereby, moderating rates in that month. As monetary conditions tightened, short-term rates rose in March but moderated slightly in April and May in response to significant OMO maturities and statutory revenue payments to the three tiers of government. However, the rates trended upward in June 2012 as banking system liquidity became tight following delay in the distribution of statutory revenue and the effect of OMO conducted in the preceding month.

*The thrust of exchange rate policy remained the need to engender a stable exchange rate of the naira around the mid-point of N155/US\$ with a band of +/- 3 per cent.*

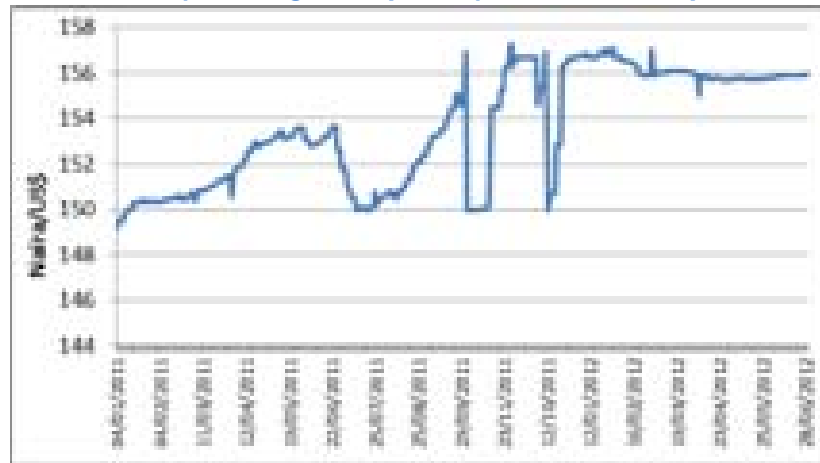
The high rates recorded towards the end of the review period were consistent with the tight monetary policy stance since the third quarter of 2011, which encouraged a shift in DMB's composition of assets portfolio in favour of high yielding short-term treasury instruments and CBN securities (figure 4.1).

### 4.2 The Foreign Exchange Market

The thrust of exchange rate policy remained the need to engender a stable exchange rate of the naira around the mid-point of N155/US\$ with a band of +/- 3 per cent. The Bank continued to respond to the persistent foreign exchange demand pressure to keep the exchange rate within the band.



**Figure 4.4**  
Daily Exchange Rate (January 2011 – June 2012)



*The depreciation in the spot rates across all segments of ...market was attributed to demand pressure driven partly by the exit of offshore investors...*

#### 4.2.1 Spot Rate

The spot rate at the official window of the foreign exchange market, the wDAS, averaged N157.65/US\$ in the first half of 2012 compared with the average N154.51/US\$ in the second half of 2011 and N153.21/US\$ in the corresponding period of 2011, representing depreciations of 2.00 and 2.80 per cent, respectively.

In the interbank foreign exchange market (IFEM), the spot rate averaged N159.31/US\$ compared with N157.27/US\$ in the second half of 2011 and N154.49/US\$ in the corresponding period of 2011. The movement in rates showed depreciations of 1.27 and 3.02 per cent in both periods, respectively. Similarly, spot rates at the BDC segment averaged N161.23/US\$ in the first half of 2012 compared with N161.66/US\$ in the second half of 2011 and N156.96/US\$ in the corresponding period of 2011, representing an appreciation of 0.27 and a depreciation 2.46 per cent, respectively.

The depreciation in the spot rates across all segments of the foreign exchange market was attributed to demand pressure driven partly by the exit of offshore investors from the local debt market, and the resurgence of demand from some companies remitting dividends to their home countries. This was, in addition to foreign exchange requests of importers

outside the official window. Consequently, the spread between the wDAS and BDC rates stood at N5.09 in December 2011 before increasing to N5.99 in June 2012 (Table 4.2).

**Table 4.2**  
**Average Monthly Spot Exchange Rates (N/US\$)**  
**(January 2011 – June 2012)**

DATE	CBN	IFEM	BDC
Jan-11	151.55	152.47	156.13
Feb-11	151.94	152.86	155.11
Mar-11	152.51	155.21	157.09
Apr-11	153.97	154.60	157.05
May-11	154.80	156.17	158.05
Jun-11	154.50	155.65	158.32
<b>2011: H1 Average</b>	<b>153.21</b>	<b>154.49</b>	<b>156.96</b>
Jul-11	151.86	152.41	163.71
Aug-11	152.72	153.79	163.10
Sep-11	155.26	156.70	158.23
Oct-11	153.26	159.83	161.25
Nov-11	155.77	158.83	160.35
Dec-11	158.21	162.17	163.30
<b>2011: H2 Average</b>	<b>154.51</b>	<b>157.29</b>	<b>161.66</b>
<b>2011 Average</b>	<b>153.54</b>	<b>155.89</b>	<b>159.31</b>
Jan-12	158.39	161.31	164.62
Feb-12	157.87	158.59	160.85
Mar-12	157.59	157.72	159.41
Apr-12	157.33	157.44	159.37
May-12	157.28	158.46	159.67
Jun-12	157.44	162.33	163.43
<b>2012: H2 Average</b>	<b>157.65</b>	<b>159.31</b>	<b>161.23</b>

*The 1-month forward rate averaged N156.27/US\$ in the first half of 2012, compared with the average of N154.45/US\$ in the second half of 2011*

#### 4.2.2 Forward Rates

The CBN continued with the foreign exchange forward transactions with authorized dealers in expectation that it would reduce speculative demand that exerted sustained pressure on the naira. The 1-month forward rate averaged N156.27/US\$ in the first half of 2012, compared with the average of N154.45/US\$ in the second half of 2011 and N153.73/US\$ in the corresponding period of 2011, indicating a

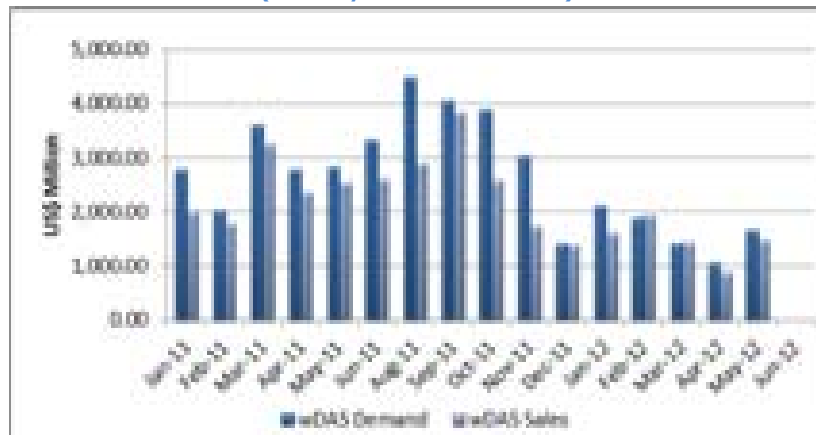
depreciation of 1.16 and 1.63 per cent, respectively. Similarly, the average forward rate for 2-month tenor was N156.27/US\$ in the review period as against N155.95/US\$ in the second half of 2011 and N154.95/US\$ in the corresponding period of 2011, reflecting a depreciation of 0.20 and 0.84 per cent, respectively. The forward rate for 3-month tenor transactions recorded an appreciation of 1.14 per cent to an average of N156.38/US\$ in the first half of 2012, compared with an average of N158.17/US\$ in the second half of 2011.

**Table 4.3**  
**Average Monthly Foreign Exchange Forward Rates (N/US\$)**  
**(March 2011 – June 2012)**

DATE	1-MONTH	2-MONTH	3-MONTH
Mar-11	152.43	153.85	154.27
Apr-11	153.75	154.30	154.46
May-11	154.47	155.52	156.71
Jun-11	154.29	155.49	153.45
<b>2011: 1<sup>st</sup> Half Average</b>	<b>153.73</b>	<b>154.95</b>	<b>154.81</b>
Jul-11	151.57	152.97	
Aug-11	152.4	153.75	154.91
Sep-11	154.47	155.54	156.47
Oct-11	155.68	156.99	158.34
Nov-11	153.75	155.48	158.06
Dec-11	158.85	160.99	163.05
<b>2011: 2<sup>nd</sup> Half Average</b>	<b>154.45</b>	<b>155.95</b>	<b>158.17</b>
Jan-12	157.16	157.16	-
Feb-12	156.81	156.76	156.88
Mar-12	156.09	156.06	-
Apr-12	155.88	155.93	-
May-12	155.80	155.83	-
Jun-12	155.88	155.88	155.88
<b>2012: 1<sup>st</sup> Half Average</b>	<b>156.27</b>	<b>156.27</b>	<b>156.38</b>

The average demand at the wDAS forward market decreased by 1.40 per cent from US\$520.42 million in the second half of 2011 to US\$513.12 million in the review period. Similarly, total sales by the CBN decreased by 13.68 per cent from US\$367.23 million in the second half of 2011 to US\$317.01 million in the first half of 2012.

**Figure 4.5**  
**Demand and Sale of Foreign Exchange at wDAS Forwards**  
**(January 2011 – June 2012)**

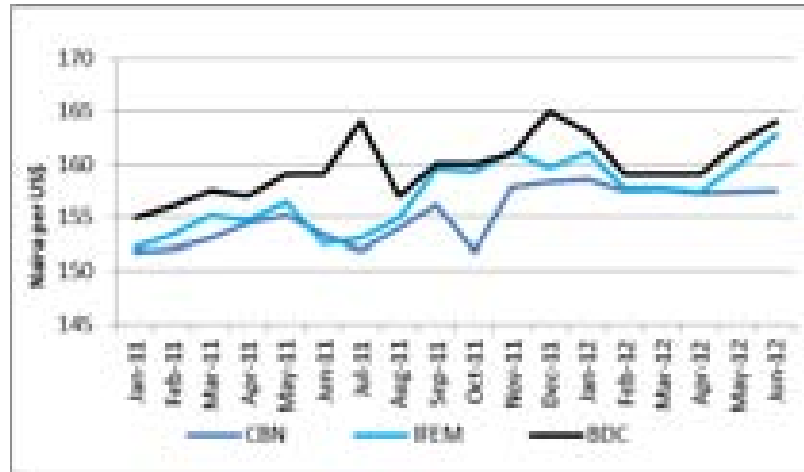


### 4.2.3 End-Period Exchange Rate

In the first half of 2012, there was mixed performance in all segments of the market. At the wDAS, the naira appreciated by 0.5 per cent from N158.27/US\$ at end-December 2011 to N157.50/US\$ at end-June 2012. It however, depreciated by 2.7 per cent from N153.31/US\$ to N157.50/US\$ at end-June, 2012 respectively, when compared with the corresponding period of 2011 (Table 4.4).

Similarly, the naira appreciated by 0.6 per cent from N165.00/US\$ at end-December 2011 to N164.00/US\$ at the BDC segment at end-June 2012, but depreciated by 3.05 per cent when compared with the corresponding period of 2011. At the interbank segment, the naira depreciated to N162.85/US\$ at end-June 2012 from N159.7/US\$ at end-December 2011 and N153.00/US\$ at end-June 2011, representing depreciations of 1.93 and 6.34 per cent, respectively (Table 4.4).

**Figure 4.6**  
**End-Month Exchange Rate of the Naira (Jul. 2010 - Dec. 2011)**



**Table 4.4**  
**End-Month Exchange Rates Movements at Various**  
**Segments of the Market, January 2011 – June 2012 (N/US\$)**

DATE	CBN	IFEM	BDC
Jan-11	151.85	152.20	155.00
Feb-11	152.07	153.35	156.00
Mar-11	153.04	155.22	157.50
Apr-11	154.45	154.72	157.00
May-11	155.13	156.40	159.00
Jun-11	153.31	152.52	159.00
Jul-11	151.96	153.00	164.00
Aug-11	153.92	155.00	157.00
Sep-11	156.15	159.60	160.00
Oct-11	151.75	159.35	160.00
Nov-11	157.87	161.20	161.00
Dec-11	158.27	159.70	165.00
Jan-12	158.62	161.16	163.00
Feb-12	157.46	157.75	159.00
Mar-12	157.57	157.72	159.00
Apr-12	157.26	157.40	159.00
May-12	157.31	159.85	162.00
Jun-12	157.50	162.85	164.00

The Nominal Effective Exchange Rate (NEER) index decreased to N99.27 at end-June 2012,...

#### 4.2.4 Nominal and Real Effective Exchange Rate Indices

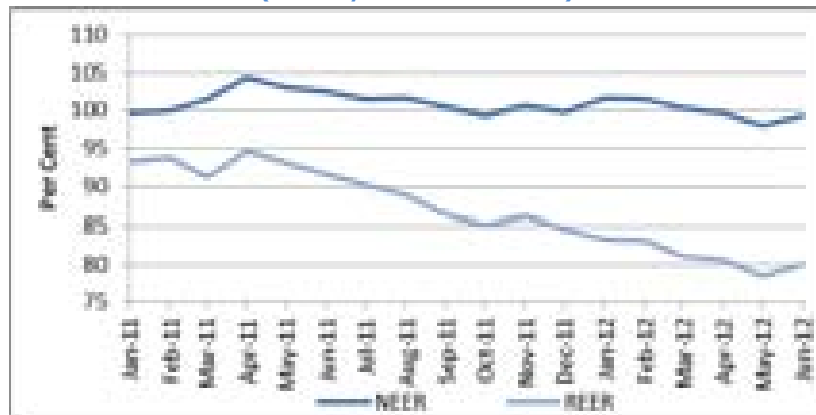
The Nominal Effective Exchange Rate (NEER) index decreased to N99.27 at end-June 2012, representing appreciations of 0.46 and 3.19 per cent from the N99.73 at end-December 2011 and N102.54 at end-June 2011, respectively. The Real Effective Exchange Rate (REER) index also fell to N79.98 at end-June 2012, indicating 5.41 and 12.67 per cent drop from N84.56 at end-December 2011 and N91.60 at end-June 2011, respectively (Table 4.5 and Figure 4.7).

On the average, both the NEER and REER decreased at end-June 2012, when compared with the level at end-December 2011, reflecting a real exchange rate appreciation relative to the currencies of Nigeria's major trading partners.

**Table 4.5**  
Nominal and Real Effective Exchange Rates Indices  
(January 2011 – June 2012)

DATE	NEER	REER
Jan-11	99.72	93.31
Feb-11	99.90	93.73
Mar-11	101.55	91.20
Apr-11	104.28	94.65
May-11	102.99	93.07
Jun-11	102.54	91.60
<b>2011: 1<sup>st</sup> Half Average</b>	<b>101.83</b>	<b>92.93</b>
Jul-11	101.49	90.22
Aug-11	101.62	88.82
Sep-11	100.41	86.46
Oct-11	99.24	85.08
Nov-11	100.73	86.26
Dec-11	99.73	84.56
<b>2011: 2<sup>nd</sup> Half Average</b>	<b>100.54</b>	<b>86.90</b>
Jan-12	101.69	83.27
Feb-12	101.41	83.00
Mar-12	100.29	81.03
Apr-12	99.66	80.49
May-12	97.94	78.49
Jun-12	99.29	80.00
<b>2011: 1<sup>st</sup> Half Average</b>	<b>100.04</b>	<b>81.04</b>

**Figure 4.7**  
**Nominal and Real Effective Exchange Rates Indices**  
**(January 2010 – June 2012)**



#### 4.2.5 Demand and Supply of Foreign Exchange

Total demand for foreign exchange at the wDAS in the review period decreased by 45.23 per cent to US\$10,964.17 million from US\$20,020.37 million recorded in the second half of 2011. Compared with the US\$17,405.43 million demanded at end-June 2011, the demand for foreign exchange fell by 38.77 per cent. The total supply of foreign exchange at the wDAS amounted to US\$10,414.10 million in the first half of 2012, compared with US\$15,146.87 million recorded in the second half of 2011 and US\$14,638.04 million at end-June 2011, representing decreases of 31.25 and 28.86 per cent, respectively (Table 4.6).

The various policy actions undertaken by the Bank in the last quarter of 2011 were sustained in the first half of 2012, and culminated in reduced demand at the official window and huge inflows into the foreign exchange market, especially through investment in government securities. Consequently, demand for foreign exchange at the wDAS was low compared with the level in the preceding period. The period also experienced an increase in the price of crude oil (Nigeria's major source of foreign exchange earnings). Foreign exchange reserves also grew during the period as a direct consequence of reduced demand/intervention by the Bank.

However, by mid-May 2012, foreign exchange demand at the wDAS re-surfaced as private inflows (especially sales by oil companies) reduced. In order to ensure exchange rate stability in the face of renewed pressure at the foreign exchange market, the Bank increased sales at the bi-weekly auctions to US\$400.00 million, from US\$150.0 million. Also, the Bank commenced special interventions in the interbank market and sold the sum of US\$774.20 and US\$666.0 million in May and June 2012, respectively. The forwards segment of the market helped to absorb some of the demand at the spot market.

**Table 4.6**  
**Foreign Exchange Demand and Supply Rates Indices**  
**(US\$ million)**

DATE	wDAS Demand	wDAS Sales
Jan-11	2,800.42	2,000.00
Feb-11	2,041.09	1,794.85
Mar-11	4,080.28	3,274.38
Apr-11	2,780.41	2,375.58
May-11	2,878.43	2,549.89
Jun-11	3,325.53	2,643.34
<b>2011: 1<sup>st</sup> Half Total</b>	<b>17,906.16</b>	<b>14,638.04</b>
Jul-11	3,065.41	2,643.34
Aug-11	4,504.49	2,899.05
Sep-11	4,081.18	3,850.00
Oct-11	3,899.58	2,607.00
Nov-11	3,054.43	1,749.62
Dec-11	1,415.28	1,397.86
<b>2011: 2<sup>nd</sup> Half Total</b>	<b>20,020.37</b>	<b>15,146.87</b>
Jan-12	2,134.00	1,640.65
Feb-12	1,891.96	1,942.18
Mar-12	1,426.45	1,452.75
Apr-12	1,052.88	891.52
May-12	1,681.26	1,487.00
Jun-12	2,777.62	3,000.00
<b>2012: 1<sup>st</sup> Half Total</b>	<b>10,964.17</b>	<b>10,414.10</b>

#### 4.2.6 Foreign Exchange Flows

Gross foreign exchange inflow into the economy was US\$22,140.75 million in the first half of 2012, compared with



..foreign exchange flows resulted in a net inflow of US\$2,768.12 million, reflecting an improvement over the net outflow of US\$612.77 million in the second half of 2011

US\$27,631.39 million and US\$19,547.33 million in the second half and the corresponding period of 2011, representing a decrease of 19.87 and an increase of 13.11 per cent, respectively (Figure 4.8 and Table 4.7). Foreign exchange outflow decreased from US\$28,244.16 million in the second half of 2011 to US\$19,372.63 million in the first half of 2012 (or by 31.41 per cent). Relative to the corresponding period of 2011, total outflow fell by 5.64 per cent.

In the first half of 2012, foreign exchange flows resulted in a net inflow of US\$2,768.12 million, reflecting an improvement over the net outflow of US\$612.77 million in the second half of 2011 and the US\$956.19 million in the corresponding period of 2011 (Table 4.7). This development reflected the reduced funding of wDAS.

**Table 4.7**  
**CBN Monthly Foreign Exchange Flows**  
**(US\$ million)**

DATE	INFLOW	OUTFLOW	NET FLOW
Jan-11	3,435.55	2,805.78	629.77
Feb-11	3,164.68	2,768.68	396.00
Mar-11	4,119.17	3,985.95	133.22
Apr-11	2,495.61	3,439.70	-944.09
May-11	2,896.12	3,657.16	-761.04
Jun-11	3,463.20	3,873.25	-410.05
<b>2011: 1<sup>st</sup> Half</b>	<b>19,574.33</b>	<b>20,530.52</b>	<b>-956.19</b>
Jul-11	4,647.69	3,826.89	820.80
Aug-11	4,356.59	4,234.08	122.51
Sep-11	5,323.46	6,087.81	-764.35
Oct-11	4,915.31	5,345.96	-430.65
Nov-11	4,256.05	5,082.29	-826.24
Dec-11	4,132.29	3,667.13	465.16
<b>2011: 2<sup>nd</sup> Half</b>	<b>27,631.39</b>	<b>28,244.16</b>	<b>-612.77</b>
<b>2011 Total</b>	<b>47,205.72</b>	<b>48,774.68</b>	<b>-1,568.96</b>
Jan-12	4,307.02	2,945.80	1,361.22
Feb-12	3,546.16	3,902.27	-356.11
Mar-12	4,266.63	2,912.43	1,354.20
Apr-12	3,242.89	1,754.89	1,488.00
May-12	3,627.10	3,256.97	370.13
Jun-12	3,150.95	4,600.27	-1,449.32
<b>2012: 1<sup>st</sup> Half</b>	<b>22,140.75</b>	<b>19,372.63</b>	<b>2,768.12</b>

**Figure 4.8**  
**Foreign Exchange Flows (January 2011 – June 2012)**



*The capital market was weighed down by profit taking activities of investors especially in the equity segment*

### 4.3 Capital Market

The capital market was weighed down by profit-taking activities of investors (especially in the equities segment) and inadequate market liquidity; particularly, in the absence of trading at the long-end of the bonds market. The situation also reflected the global trend with major markets reporting relatively weak indices in the period under review. Slow growth in emerging market economies in Asia and South America notably Brazil, India and China arising from increases in investor-risk-aversion and perceived growth uncertainty, led to equity price decreases, capital outflows and higher yield on sovereign instruments.

#### 4.3.1 Equities Market

The NSE All-Share Index (ASI) increased by 4.19 per cent to 21,599.56 at end-June 2012, from its level of 20,730.63 at end-December 2011, but decreased by 13.53 per cent, when compared with the first half of 2011. Market Capitalization (MC) (equities) increased by 5.55 per cent to N6.90 trillion at end-June 2012 from N6.53 trillion at end-December 2011, but decreased by 13.67 per cent when compared with the N7.99 trillion recorded at end-June 2011 (Table 4.8 and Figure 4.9).

This development mirrored the trend in advanced and emerging equity markets and was traced to the economic

slowdown in the euro area and the U.S. The euro area had been at the centre of international financial market distress, caused by heightened political and financial uncertainty in Greece, banking sector crisis in Spain, misgivings about governments' ability to deliver on fiscal adjustment and reforms as well as the extent of preparedness of other EU countries to provide bail-out funds. In the U.S, fiscal problems, weak economic data (especially high rate of unemployment), declining consumer confidence and reduction in the U.S. growth projections by the Federal Reserve Bank system, weakened investor-appetite for equities.

**Table 4.8**  
**NSE All-Share Index (ASI) and Market Capitalization (MC)**  
**(July 2011 – June 2012)**

<b>Date</b>	<b>All-Share Index (ASI)</b>	<b>Market Capitalization (Equities) (N' Trillion)</b>
<b>Jun-11</b>	24,980.20	7.99
<b>Jul-11</b>	23,826.99	7.62
<b>Aug-11</b>	21,497.61	6.88
<b>Sep-11</b>	20,373.00	6.50
<b>Oct-11</b>	20,934.96	6.63
<b>Nov-11</b>	20,003.36	6.29
<b>Dec-11</b>	20,730.63	6.53
<b>Jan-12</b>	20,875.83	6.58
<b>Feb-12</b>	20,123.51	6.34
<b>Mar-12</b>	20,652.47	6.55
<b>Apr-12</b>	22,045.66	7.03
<b>May-12</b>	22,066.40	7.04
<b>Jun-12</b>	21,599.56	6.90

Source: NSE

**Figure 4.9**  
NSE ASI and MC, June 2011 – June 2012



Source: NSE

**Figure 4.10**  
NSE ASI and MC, January 2012 – June 2012



Source: NSE

The increase in the ASI and MC in the later part of the first half were mainly due to improved liquidity and strong market fundamentals. This reflected in the improved performance of listed companies with the release of their Annual (2011) and First Quarter (2012) financials as well as the announcement of market makers by the Nigerian Stock Exchange (NSE).

**4.3.2 Market Turnover**

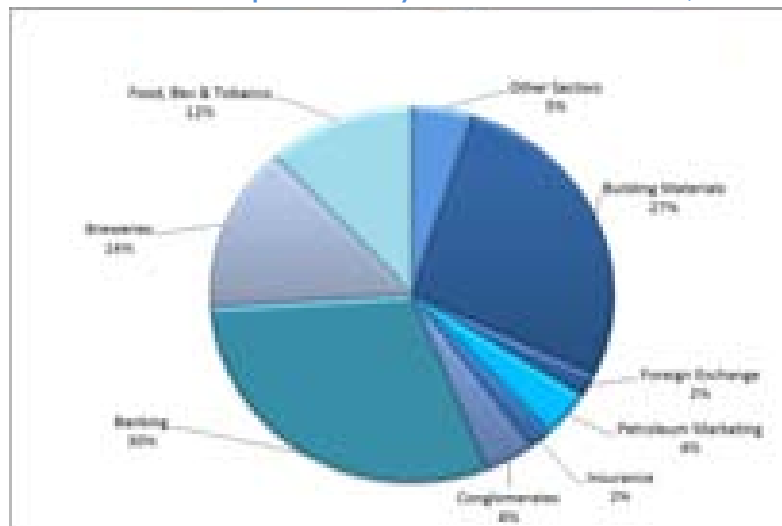
Aggregate stock market turnover in the first half of 2012 was 52.75 billion shares valued at N789.34 billion, exchanged in 427,848 deals. This compared with 40.06 billion shares valued at N262.75 billion, exchanged in 497,025 deals in the second half of 2011. There was a turnover of 49.52 billion shares valued at N372.70 billion in the first half of 2011. Relative to the second half of 2011, market turnover rose by 31.7 per cent in the review period and by 6.52 per cent, when compared with the corresponding period of 2011.

*The banking sector was the most capitalized with its overall share of the market rising to 30.0 per cent at end-June 2012 from 28.0 per cent at end-December 2011*

**4.3.3 Sectoral Contribution to Equities Market Capitalization**

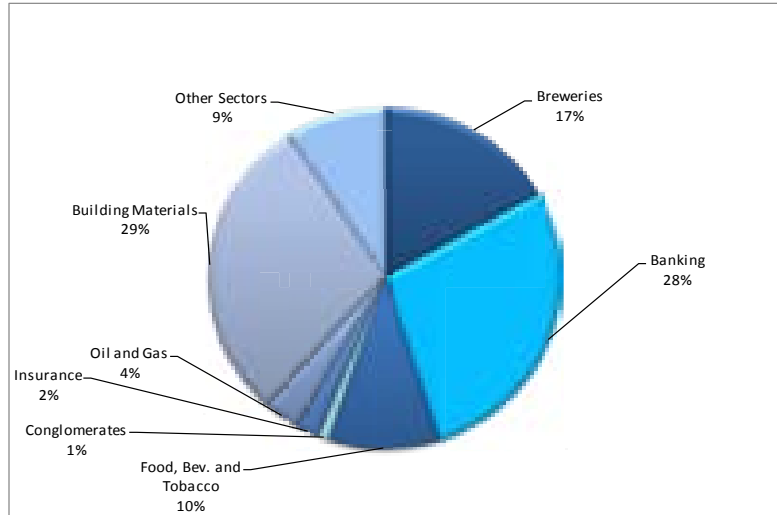
The banking sector was the most capitalized with its overall share of the market rising to 30.0 per cent at end-June 2012 from 28.0 per cent at end-December 2011. Compared with the 30.0 per cent at end-June 2011, the sector's share of market capitalization remained unchanged. Other leading sectors were the breweries and food, beverages and tobacco with respective market shares of 16.0 and 10.0 per cent, respectively at end-June 2012.

**Figure 4.11**  
**NSE Market Capitalisation by Sector as at End – June, 2011**



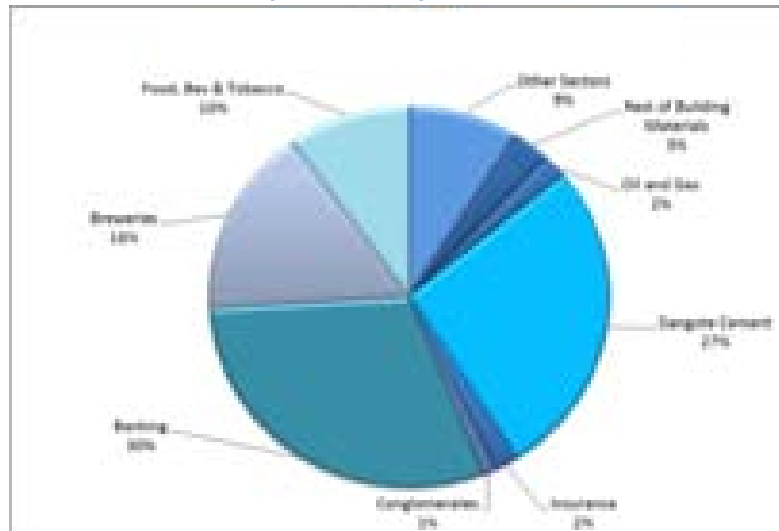
Source: NSE

**Figure 4.13**  
**NSE Market Capitalisation by Sector as at End-December, 2011**



Source: NSE

**Figure 4.14**  
**NSE Market Capitalisation by Sector as at June 29, 2012**



Source: NSE

#### 4.3.4 Bonds Market

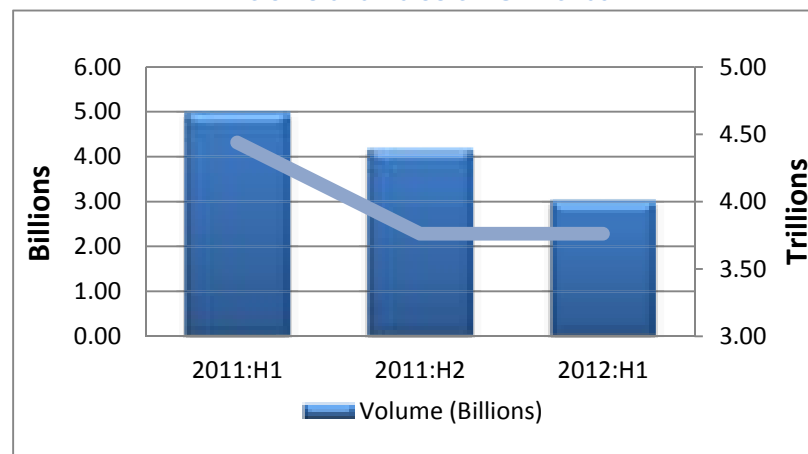
The FGN bonds market maintained the same momentum in the first half of 2012 as in the preceding half of 2011. The value of activities remained at N3.76 trillion both in the second half of

2011 and first half of 2012. It however, dropped by 15.3 per cent when compared with the corresponding period of 2011.

#### 4.3.4.1 Federal Government (FGN) Bonds

Total transactions in FGN bonds in the over-the-counter (OTC) market in the first half of 2012 was 3.04 billion units valued at N2.62 trillion in 20,357 deals, compared with 4.19 billion units valued at N3.76 trillion in 29,625 deals in the second half of 2011 and a turnover of 5.01 billion units worth N4.44 trillion in 37,053 deals recorded in the corresponding period of 2011 (Figure 4.14). The decline in the OTC market was largely attributed to the trading of only sixteen FGN bonds (on average) out of the twenty six issues outstanding.

**Figure 4.15**  
Volume and Value of FGN Bonds



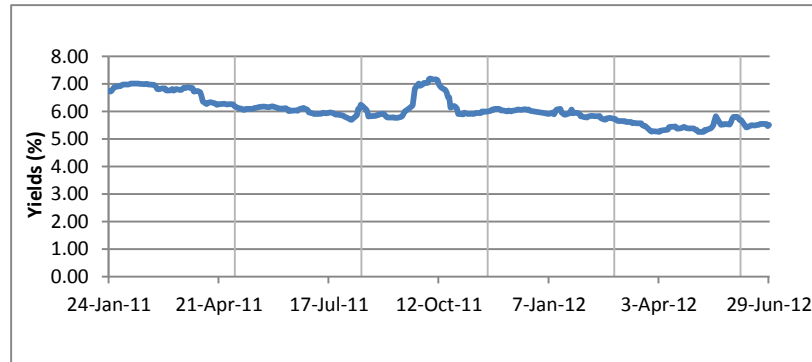
Source: NSE

#### 4.3.4.2 FGN Eurobond

The Federal Government of Nigeria's Eurobond continued to be traded in the review period. Yields on the bonds decreased from 6.03 per cent at end-December 2011 to 5.52 per cent at end-June 2012. The decrease in the Eurobond yield reflected improved confidence in the country's risk profile by foreign investors. Weak global economic and financial conditions and in particular, investor-concern about the euro area sovereign debt crisis continued to facilitate the redirection of capital flows in favour of emerging market and developing countries. In the domestic economy, measures taken by the Central Bank

to stabilize the exchange rate and increase the stock of external reserves also assisted in boosting investor-confidence (figure 4.15).

**Figure 4.16**  
**10-year U.S. Dollar-denominated Bond Yields for Nigeria**  
**(January 24, 2011 – June 29, 2012)**



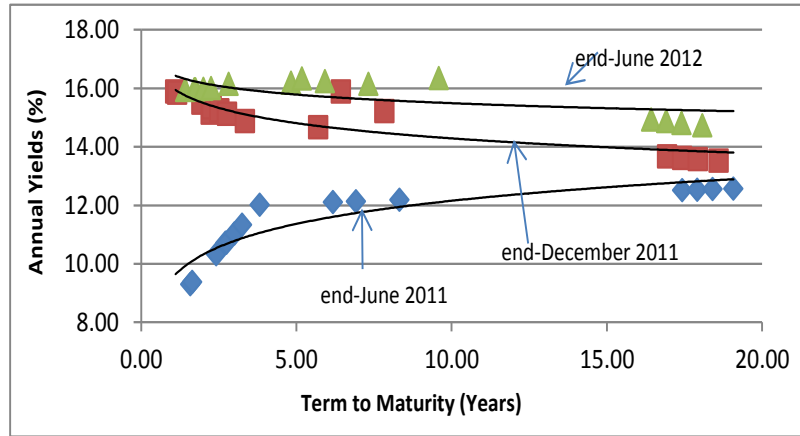
Source: Bloomberg

#### 4.3.4.3 Yields on Federal Government Bonds

The FGN bonds yield curve at end-June 2012 shifted outwards by 89 basis points compared with the position at end-December 2011 and also by 435 basis points compared with the level at end-June 2011 (Figure 4.16). The upward shift in the yield curve was traceable to the prevailing MPR of 12.0 per cent within the period. Yields on all FGN bonds were above the 12.9 per cent inflation rate indicating positive returns on FGN bonds as at end-June 2012.



**Figure 4.17**  
**FGN Bond Yield Curves**  
**(end-June 2011 vs end-December 2011 vs end-June 2012)**



Source: Bloomberg

#### 4.3.4.4 State Government Bonds

The total value of state government bonds issued in the first half of 2012 was N341.0 billion, compared with the N84.0 billion issued in the second half of 2011. The development was traced to the listing of the Ekiti State N20.0 billion, fixed rate development bond and the Benue State N13.0 billion fixed rate development bond.

#### 4.3.4.5 Corporate Bonds

In the first half of 2012, the value of outstanding corporate bonds dropped marginally to N1.39 trillion when compared with N1.4 trillion in the second half of 2011 despite the listing of 3 new bonds namely: N35.0 billion 14.0 per cent Medium Term Notes 2018 series 2 in favour of United Bank for Africa Plc, 11.50 per cent LCW Oct. 2014 (Lafarge WAPCO) and Chellarams Plc bond (MPR + 5 per cent Feb. 2019) all issued within the review period.



## CHAPTER 5

### ECONOMIC OUTLOOK

#### 5.1 Overview

*Global economic recovery in the first half of 2012 weakened as shown by the sustained stress on financial markets..*

Global economic recovery in the first half of 2012 weakened as shown by the sustained stress in the financial markets, sovereign debt crisis in the euro area and general investor-apaty in most countries across the world. The slowdown was more pronounced in the second quarter, resulting in rising unemployment in most advanced and emerging market economies. Specifically, the political and financial situation in Greece, banking sector illiquidity in Spain, and doubts about the ability of the fiscal authorities to deliver on promised adjustments tended to worsen the already fragile global economic situation. The spillover effects of these developments were felt in form of reduced exports and output contraction in the emerging and developing economies.

Global output growth was estimated at 2.29 per cent for the first half of 2012<sup>2</sup>. In the second half of 2012, however, growth would depend on efforts to contain uncertainties in the euro area, ongoing banking sector deleveraging, improving liquidity conditions in advanced countries and strengthening capacity in developing countries. Overall, global output in 2012 may remain depressed as downside risks such as political unrest in the Middle East and North Africa (MENA); rising global energy and food prices; and financial system fragilities in euro area persist.

*.. rising security and other infrastructure challenges could, combine with the less ambient external environment to keep inflationary pressures elevated*

The outlook for the domestic economy appears mixed in the short-to medium-term. While the on-going reforms and the renewed drive to attract foreign investments into the economy could impact positively on growth, rising security and other infrastructure challenges could combine with the less ambient external environment to keep inflationary pressures elevated.

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<sup>2</sup> Quarterly and half year data were obtained from Bloomberg, while annual data were from the WEO.

*Global output growth in the first half of 2012 was estimated to have declined to 2.29 per cent from 2.77 per cent recorded in the second half of 2011....*

### 5.1.1 Global Output<sup>3</sup>

Global output growth in the first half of 2012 was estimated to have declined to 2.29 per cent from 2.77 per cent recorded in the second half of 2011 and was projected to increase to 2.39 per cent in the second half of the year. The outlook for the global economy in the second half of 2012 is premised on the possibility of improvement in market sentiments following efforts to resolve the sovereign debt and fiscal consolidation crisis in the euro area. Growth in the advanced economies was 1.40 per cent, down from 1.76 per cent in the second half of 2011 and was expected to decelerate further to 1.22 per cent in the second half of 2012. In the emerging and developing economies, growth was 6.63 per cent in the second half of 2011 as against 6.50 per cent in the first half of 2012. In Developing Asia, growth declined to 6.36 per cent in the first half of 2012 from 7.09 per cent in the second half of 2011 and was projected at 7.25 per cent in the second half of 2012. Similarly, in Latin America and the Caribbean countries, output growth decelerated from 3.56 per cent in the second half of 2011 to 2.91 per cent in the first half of 2012 and was projected to improve to 3.84 per cent in the second half.

Provisional data from the World Economic Outlook (WEO) indicate that annual output growth for 2012 in the advanced countries would be 1.4 per cent; Emerging Market and Developing Countries (EMDCs), 5.6 per cent; Developing Asia, 7.1 per cent; Latin America and the Caribbean, 3.4 per cent; MENA, 5.5 per cent and sub-Saharan Africa, 5.4 per cent (Table 5.1).

*Emerging and Developing economies are clouded with uncertainties from the external developments.. outlook for sub-Saharan African countries remained robust,..*

EMDCs are also clouded with uncertainties from external developments. Export prospects have been dampened by dwindling demand in the advanced economies just as capital inflows into these economies have surged by the default of financial system weakness in the advanced economies. This situation could persist in the near-term, thereby, intensifying appreciation pressure on exchange rates and current account in these countries. The outlook for sub-Saharan African countries

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<sup>3</sup> Quarterly and half year data were obtained from Bloomberg, while the annual data were from the WEO

remained robust, riding on high commodity prices, fresh investments in new mineral exploration and friendlier investment climate. In the same vein, the outlook for the MENA region seems promising against the background of serious disruptions experienced in 2011. The region could witness a return of foreign direct investment (FDI) flow in the foreseeable future. However, the Syrian crisis and the unstable political situation in Libya could affect the region's outlook. Also, Iran's nuclear programme and the United Nations (UN)-backed sanctions may further depress the prospects for growth in the region.

**Table 5.1**  
**World Economic Outlook (WEO)**

	2009	2010	2011	2012	2013
<b>A. World Output</b>					
World Output	-0.7	5.3	3.9	3.5	3.9
<b>Advanced Economies</b>	-3.7	3.2	1.6	1.4	1.9
USA	-3.5	3.0	1.7	2.0	2.3
Euro Area	-4.3	1.9	1.5	-0.3	0.7
Japan	-6.3	4.4	-0.7	2.4	1.5
UK	-4.9	2.1	0.7	0.2	1.4
Canada	-2.8	3.2	2.4	2.1	2.2
Other Advanced Economies	-1.1	5.8	3.2	2.4	3.4
<b>Emerging &amp; Developing Economies</b>	<b>2.8</b>	<b>7.5</b>	<b>6.2</b>	<b>5.6</b>	<b>5.9</b>
Central and Eastern Europe	-3.6	4.5	5.3	1.9	2.8
Commonwealth of Independent States	-6.4	4.8	4.9	4.1	4.1
Developing Asia	7.2	9.7	7.8	7.1	7.5
Latin America and the Caribbean	-1.7	6.2	4.5	3.4	4.2
Middle East and North Africa	2.6	5.0	3.5	5.5	3.7
Sub-Saharan Africa	2.8	5.3	5.2	5.4	5.3
<b>B. Commodity Prices (US' Dollars)</b>					
Oil	-36.3	27.9	31.6	-2.1	-7.5
Non-fuel	-15.7	26.3	17.8	-12.0	-4.3
<b>C. Consumer Prices</b>					
Advanced Economies	0.1	1.5	2.7	2.0	1.6
Emerging & Developing Economies	5.2	6.1	7.2	6.3	5.6

Sources: IMF World Economic Outlook Update, July 2012

*Global inflation moderated to 2.87 per cent in the first half of 2012 from 3.70 per cent...*

### 5.1.2 Global Inflation

Global inflation moderated to 2.87 per cent in the first half of 2012 from 3.70 per cent recorded in the second half of 2011, largely due to falling commodity and energy prices. Global inflation is projected to slow further to 2.42 per cent in the second half of 2012 as a result of declining demand, falling commodity prices and weakening global economy. In the advanced economies, inflation averaged 2.10 per cent in the first half of 2012 as against 2.73 per cent in the second half of 2011, and could further decline to 1.75 per cent in the second half of 2012. Similarly, inflation in the U.S. was 2.47 per cent in the first half of 2012 down from 3.55 per cent in the second half of 2011, and is projected to further ease to 1.95 per cent in the second half of 2012. In sub-Saharan Africa, a combination of pressures arising from strong domestic and foreign exchange demand coupled with rising food prices could accentuate consumer price inflation in the second half of 2012.

*..projected decline in oil prices is largely due to high prospects of further slowdown in economic activities in the second half of 2012*

### 5.1.3 Global Oil Prices

The Organization of Petroleum Exporting Countries (OPEC) basket price of crude oil averaged US\$112.05 per barrel in the first half of 2012, up from US\$107.96 per barrel in the second half of 2011, representing an increase of 3.79 per cent. The reviewed IMF baseline oil price projection for 2012 of US\$101.80 per barrel is lower than the average price at end-June 2012. The projected decline in oil prices is largely due to high prospects of further slowdown in economic activities in the second half of 2012.

*..overall growth outlook for the domestic economy in the second half of 2012 remains fairly optimistic*

### 5.1.4 Domestic Output Growth

The overall growth outlook for the domestic economy in the second half of 2012 remains fairly optimistic. Provisional data from the NBS shows output growth of 6.37 per cent in the first half of 2012 as against 7.54 per cent recorded in the second half of 2011. The NBS estimates growth of the domestic economy to slow to 6.5 per cent in 2012. This projection is based on anticipated slowdown in the global economy, loss of N207.41 billion in national output during the oil subsidy strike in January 2012 and security challenges in most parts of the country. However, expected increase in electricity generation following the ongoing power sector reforms, conclusion of the

banking sector reforms, implementation of Federal Government's transformation initiatives particularly in agriculture and growth in the non-oil sector are expected to drive output in 2012 and beyond.

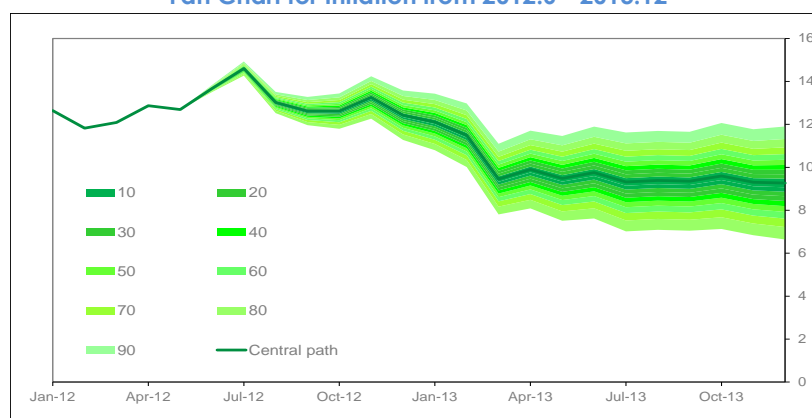
## 5.2 Outlook for Inflation and Monetary Policy in 2012

### 5.2.1 Inflation Outlook

Inflation at the end of the first half of 2012 was 12.9 per cent up from 10.31 per cent in the second half of 2011. Staff forecast suggests that headline inflation rate would lie between 12.57-12.67 and 12.34-12.51 per cent in September 2012 and December 2012, respectively, based on 90.0 per cent confidence limits. At a higher confidence level, headline inflation would lie between 11.96-13.28 and 11.27 -13.58 per cent in September 2012 and December 2012, respectively. However, by December 2013, the rate could moderate to between 9.07 – 9.47 or 6.64 – 11.9 per cent.

The upside risks to this projections include fiscal injections in relation to the 2012 budget and unexpected natural disasters like flood, drought in parts of the country, the second round effects of the partial removal of subsidy on PMS in January 2012, rising global commodity prices due to drought in different parts of the world, the implementation of the new tariff regimes on imported food products such as rice, wheat and flour as well as the upward review of electricity tariff in June 2012.

**Figure 5.1**  
Fan Chart for Inflation from 2012:6 - 2013:12



Source: Research Department, CBN





## APPENDICES

### Communiqué of the Monetary Policy Committee (January – June 2012)

#### Central Bank of Nigeria Communiqué No. 81 of the Monetary Policy Committee Meeting of Monday and Tuesday, January 30 and 31, 2012

The Monetary Policy Committee (MPC) met on January 30 and 31, 2012 with all 12 members in attendance to review the domestic economy in 2011 and the nature of current challenges against the background of developments in the international economic and financial environments.

At the outset, the Committee recalled that in a bid to ensure price and financial stability, the Committee, held six (6) regular meetings and one (1) extra-ordinary meeting in 2011 during which it raised the Monetary Policy Rate (MPR) six (6) times, from 6.25 to 12.0 per cent; raised the cash reserve ratio (CRR) three (3) times from 1.0 to 8.0 per cent; and the liquidity ratio (LR) once from 25.0 to 30.0 per cent. It also reduced the foreign exchange net open position of DMBs from 5.0 to 3.0 per cent, and adjusted the mid-point of the exchange rate band from N150/US\$1 to N155/US\$1. These decisions signalled to the market the Committee's clear and unambiguous commitment to the primacy of price stability as its key mandate.

#### The Global Economy

Latest projections by the International Monetary Fund (IMF) indicated that global output growth which had slackened from 5.2 per cent in 2010 to 3.8 per cent in 2011 could decelerate further to 3.3 per cent in 2012. Advanced economies are expected to record a lower rate of growth of 1.2 per cent in 2012 compared to the estimated 1.6 per cent in 2011. The US economic growth in the coming quarters would depend a great deal on growth of the euro area. The euro area is projected to record a negative growth of 0.5 per cent in 2012 essentially on account of the burden of high public debt and the fragility of the credit and financial markets. Output growth in emerging and developing economies slowed down in 2011. China, India and Brazil all posted lower growth rates in 2011 than in 2010. Sub-Saharan Africa has been a major exception to the global trend: it is estimated to have grown by 4.9 per cent in 2011 and is expected to record a higher growth of 5.5 per cent in 2012.

Inflation rates in most of the advanced economies trended upward in 2011 with the exception of Japan. In the US, UK, and Germany, inflation rose from 1.4, 3.7, and 1.7 per cent in 2010 to 3.0, 4.2, and 2.1 per cent in 2011, respectively. The

Euro-zone debt crisis worsened; leading to credit ratings downgrades, change of governments, and implementation of austerity measures, even as a few nations appeared to have entered into a recession.

The Committee felt that in the light of the expected deceleration in the economies of the country's major trading partners, and the absence of adequate commitment of most advanced economies to effectively address the fiscal imbalances and to reform their financial systems, there would be continued pressure on Nigeria's external sector in 2012. The anticipated slack in external demand would, in the view of the Committee, have to be offset by generating the needed domestic demand. This, however, would require a shift in the economic development strategy that allows greater diversification of the economy without losing sight of the need to pursue sound demand management policies.

### **Key Domestic Macroeconomic and Financial Developments Output and Prices**

Provisional data from the National Bureau of Statistics (NBS) indicated that real Gross Domestic Product (GDP) grew by 8.68 per cent in the fourth quarter of 2011 up from 6.64, 7.72, and 7.40 per cent in the 1st, 2nd and 3rd quarters, respectively. The overall GDP growth rate in 2011 was estimated by the NBS at 7.69 per cent, marginally lower than the 7.87 per cent recorded in 2010. This projection is based on the estimated third quarter and fourth quarter growth rate of 7.40 per cent and 8.68 per cent respectively. The 2012 Budget proposal assumed a growth rate of 7.2 per cent. This is in line with the latest World Bank forecast of 7.1 per cent growth for Nigeria in 2012. The Committee noted with satisfaction, the good performance of non-oil activities including agricultural and services sectors as well as the recovery in crude oil output in 2011, particularly in the fourth quarter. In the Committee's view, the opportunity to build on the robust non-oil growth with further investments in infrastructure and manufacturing and processing activities should be utilized in order to mitigate any negative impacts from the likely external shocks during the year.

The Committee also noted the NBS survey data on the rise in the unemployment rate to 23.9 per cent in 2011 from 21.4 per cent in 2010. The latest unemployment rate is considerably higher than the 12.3 per cent recorded in 2006 by the NBS survey, which suggests that the consistently high output growth during this period had failed to create adequate employment for the growing labour force.

In view of this, the Committee recommends that in addition to the structural reforms being currently pursued, emphasis should be placed on technical and

vocational education in order to produce a labour force that is compatible with the current stage of the country's development.

In 2011, the Inflation rate fluctuated within the lower double-digits range during the early part of the year, but moderated thereafter. The year-on-year headline inflation rate, which was 12.1 per cent in January 2011 rose to 12.8 per cent in March, before moderating to 10.2, 10.3, and 10.3 per cent in June, September, and December, respectively. Similarly, food inflation rose from 10.3 per cent in January 2011 to 12.2 per cent in March and thereafter moderated to 9.2, 9.5, and 11.0 per cent in June, September, and December, respectively. Core inflation also rose from 12.1 per cent in January to 12.8 per cent in March stabilizing at 11.5, 11.6, and 10.8 per cent in June, September and December, respectively.

The headline inflation rate stood at 10.3 per cent in December 2011, by far the lowest since December 2008 and lower than the average of 12.75 per cent during the period 2001-11. Food inflation, at 11.0 per cent in December 2011, was lower than its level in the preceding three years. Similarly, the year-on-year core inflation declined in 2011. At 10.8 per cent in December 2011, core inflation was marginally lower than the 10.9 per cent in December 2010 and 11.2 per cent in December 2009. The Committee noted that both food and core inflation have remained high exerting immense pressure on the headline inflation rate. The Committee was therefore of the view that while the focus on growth continues to be a key imperative, the containment of inflation equally deserves immediate attention. It noted that the inflation outlook in the short- term will be impacted by the anticipated fiscal injections in relation to the proposed 2012 budget, the recent partial deregulation of pump price of PMS, and new tariff regimes on certain food imports. The Committee has also noted comments indicating possible plans by the National Assembly to revise the budget benchmark price of oil from \$ 70 per barrel to \$75 or even \$80 per barrel. Such a measure would significantly increase expenditures especially given the already high oil output assumptions. In addition, it would reduce accretion to the Excess Crude Account (ECA) and increase the inflationary pressure already in place on the supply-side. In the event of this happening, the likelihood of further tightening during 2012 increases. The Committee would like to reaffirm its commitment to price and exchange rate stability and its determination not to pursue an accommodative policy stance. The Committee therefore, strongly supports the recommendations of the Executive for a benchmark price of a maximum of \$70 per barrel.

### Monetary, Credit and Financial Market Developments

Broad money supply (M2) growth was sluggish up to May, 2011, accelerated thereafter to 5.66, 9.50 and 15.40 per cent in June, September, and December 2011, respectively. When annualized, M2 grew by 11.32, 12.67, and 15.40 per cent in June, September and December, respectively, which hovered around the indicative growth benchmark of 13.75 per cent for 2011. Thus, M2 growth of 15.4 per cent in 2011 was higher than the 6.9 per cent growth in 2010. The significant increase in credit to the private sector as result of loan to AMCON to finance its activities was a major factor underlying growth in monetary aggregates in 2011.

The Committee noted that money market rates moved upward in 2011. The average OBB rate increased to 15.50 per cent in December from 6.22, per cent in January. Similarly, the average call rate rose to 14.09 per cent in December from 6.42, per cent in January. The rise in money market rates should be viewed in the overall context of monetary tightening stance of the Bank in 2011 through hikes in the monetary policy rate (MPR) as well as the sharp increase in the cash reserve ratio (CRR) from 4 per cent in September to 8 per cent in October. The Committee observed that monetary tightening was also used to restore stability in the foreign exchange market. In January 2012, money market rates have been hovering within a range of 12.85-15.70 per cent. Long term bond yields have tended to move in the range of 14-15 per cent.

Responding positively to the hike in policy rates, both the lending and deposits rates of deposit money banks also moved up in 2011, although substantially less in the case of the latter. The maximum lending rate increased to 23.21 per cent in December from 21.75, 22.02, 22.02 and 22.09 per cent in January, March, June and September, respectively. Also, the prime lending rate rose to 16.75 per cent in December from 15.73, 15.81, 15.76 and 15.87 per cent in January, March, June and September, respectively. The spread between the maximum lending rate and the average deposit rate which was at 19.22 percentage points in June moved up to 20.12 percentage points in December.

### External Sector Developments

Foreign exchange reserves amounted to US\$ 32.64 billion as at end December 2011, more or less flat relative to the US\$32.34 billion as at end December 2010, despite the higher oil price in 2011. Notwithstanding the high prices of Nigeria's reference crude oil (Bonny Light) which averaged US\$106.32 per barrel for the year, the limited accretion to external reserves was due to the high demand for foreign exchange in the market. The Committee noted that pressure on the exchange rate emanating from the high demand reflected the import-dependent nature of the economy, probably compounded by the activities of

speculators. The reduction in arbitrage opportunities in the oil marketing sectors combined with stronger controls in foreign exchange practices have already led to a noticeable moderation in foreign exchange net demand.

The official wDAS rate (inclusive of 1 per cent commission) moved up from N151.62 per US\$1 in January 2011 to N154.45/US\$1 in June and further to N158.21/US\$1 in December 2011. The volatility in the official rates, however, was limited with the coefficient of variation being 1.28 per cent for the year as a whole compared to 0.32 per cent in 2010. The Committee commended the CBN for its efforts at establishing stability in the market. It also urged the CBN to strive to eliminate speculative demand for foreign exchange. The Committee also noted that as at January 24, 2012, the exchange rate was N158.57/US\$1, while the foreign exchange reserves amounted to \$34.18 billion on January 27, 2012, which could finance over 6 months of imports of goods and services. The outlook for oil prices in the short-term as well as the forecast demand/supply balance, suggest that the current exchange rate band should be retained while still achieving moderate continuous accretion to reserves

#### **The Committee's Considerations**

The Committee is pleased that ahead of most African countries, Nigeria had been proactive by responding to the threats of inflation induced by fiscal spending and global food, fuel and other commodity prices as well as to the challenges of financial stability. The Committee observed that the mandate of the Bank was largely achieved, as inflation was contained within tolerable levels and the exchange rate was generally stable throughout 2011. The resolution of the banking crisis during the year was also commended. Against this background, the Committee welcomed the stated fiscal stance of the Federal Government as part of its programmed movement towards fiscal consolidation. The increased share of capital expenditure in the proposed total expenditure in 2012 is an important signal of the commitment of the Federal Government to improve the productive capacity of the economy. The Committee finds the current environment to be conducive for improved co-operation and coordination between fiscal and monetary authorities.

The Committee acknowledged that the decision to remove the fuel subsidy was a major development that took place since its last meeting in November 2011. It commended the Federal Government on the partial removal of subsidy on Premium Motor Spirit (PMS), which it noted will have salutary effects on the external reserves and exchange rate as well as on investment in oil and gas downstream sector. It further commended the Federal Government for the commitment towards the passage of the Petroleum Industry Bill (PIB) which, it

believes, would further complement the benefits of the fuel subsidy removal. On the other hand, it recognized the possible negative impact of the partial removal of fuel subsidy on the general price level and hence inflation in the short run. In this regard, it underscored the need for the speedy implementation of the palliative measures and entrenchment of social safety nets for the more vulnerable groups. However, the long-term benefits far outweigh the likely short term costs as far as inflation is concerned.

Furthermore, the Committee commended the fiscal authorities for the benchmark crude oil price of \$70 per barrel as proposed in the 2012 budget and advocated for its retention as any upward revision would tend to undermine macroeconomic stability.

The Committee considered the need to sustain the high output growth that the country has seen in recent years partly because of the slowdown in the advanced and other emerging economies and partly because of the need to generate employment in the economy. However, to help generate new jobs, it would be essential for the Federal Government to move quickly with the structural reforms such as (a) power sector reforms, (b) implementing the agricultural sector transformation programmes and the associated value chain, and (c) refocusing attention to the provision of technical and vocational training to bring about skills development that would match the needs of the economy.

The Committee underscored the need for maintaining price stability in a manner conducive to the achievement of employment-generating growth. In this connection, it observed that the announced increase in import duties on some food items by the end of June 2012 would exert further pressure on food prices which would compound the effect of increased transportation costs induced by the partial removal of the fuel subsidy on the general price level and the associated inflation expectation.

The Committee noted that historically, upward adjustments in the price of PMS have tended to have a short-term impact on the rate of inflation. A review of previous instances of adjustment in fuel prices shows that without exception, each instance is accompanied by an increase in the rate of inflation followed almost immediately by a moderation in the short - to - medium term. Staff estimates indicate that inflation in the first two quarters of 2012 would range between 11.0 per cent and 14.5 per cent, and then moderate steadily towards the single digit zone by late 2013. Real interest rates are therefore likely to remain positive on a trend basis, even if the rate of inflation were to rise briefly above the MPR in the second quarter.

Finally, the Committee recognized the current security challenges and Government's efforts to find a lasting solution through dialogue, economic measures and enhanced intelligence. It expressed confidence on the ability of Government to resolve the problem.

### **Decisions**

In the light of the above, and considering the clear impact of previous tightening on the rate of inflation and exchange rates up to December 2011, the Committee unanimously decided as follows:

1. Retain MPR at 12.0 per cent with interest rate corridor of +/- 200 basis points;
2. Retain CRR at 8.0 per cent;
3. Retain minimum liquidity Ratio of 30.0 per cent; and
4. Retain the Mid-point of exchange rate at N155/US\$1 with a band of +/-3.0 per cent.

The Committee also resolved to watch closely developments with respect to the fiscal stance and to respond appropriately if, and when, the need arises.

### **Sanusi Lamido Sanusi, CON**

Governor  
Central Bank of Nigeria

*January 31, 2012*

### **Central Bank of Nigeria Communiqué No. 82 of the Monetary Policy Committee Meeting of Monday and Tuesday March 19 and 20, 2012**

The Monetary Policy Committee (MPC) met on March 19 and 20, 2012 with 10 members in attendance to review domestic and international economic and financial conditions with a view to addressing monetary policy challenges in the short-to medium-term.

#### **The International Economic Situation**

The outlook of the international economic environment has improved slightly, when compared with 2011. The U.S. economy is showing signs of recovery and is expected to post over 2 per cent growth in 2012 compared with 1.7 per cent in 2011. There are, however, lingering global security concerns, particularly with respect to the face-off between the Iranian authorities on the one hand and the governments of the U.S., Europe and Israel on the other. An escalation of conflict may threaten global energy supplies and introduce shocks into the current environment. The Eurozone countries economic outlook remained uncertain, particularly owing to the loss of momentum in growth by the end of 2011. The Eurozone countries posted a negative growth of 0.3 per cent in Q4 compared with gains of 0.2 per cent and 0.1 per cent in the preceding two quarters. The recent estimate indicated that the euro area may post a negative growth of 0.3 per cent in 2012 against the estimated 1.4 per cent in 2011. The sovereign debt problem of the highly-indebted countries of the Euro zone, however, seems to be coming under control with supportive actions from creditors, in particular the European Central Bank (ECB) and the IMF, which also boosted liquidity and sentiment in the financial markets. The economic prospects of the United Kingdom also seem to have improved recently partly owing to the financial support given by the ECB to the financial markets and partly due to news of the incipient signs of improvement in the economy of the U.S. The changed monetary stance of the ECB has clearly provided the short term support needed to restore confidence and kick-start recovery subject to improvements in fiscal balance sheets and competitiveness in the European periphery.

In emerging economies, there is clear evidence of a slowdown. China posted 8.9 per cent growth in Q4 2011, the lowest since Q2 2009. It is expected that China's growth will slow down further in the current quarter going by the weak industrial production gains in January and February and the low retail sales. Consequently, China has revised its growth target for 2012 downward from 8.0 per cent to 7.5 per cent. In India, growth in the quarter ending December 2011 was lower at 6.1 per cent compared with 6.9 per cent in the preceding quarter. Inflation rose in February 2012 with the result that inflation in 2011-12 could well be slightly above 7 per cent. However, the latest official estimate of growth for 2012-13 is 7.6 per cent.



This is partly attributed to expected improvement in the fiscal position and somewhat relaxed monetary policy. Brazil's growth in Q4 of 2011 was 2.47 per cent and is expected to slow down further in 2012. For the year as a whole, Brazil recorded a mere 2.7 per cent as against 7.5 per cent in 2010. Inflation was 5.8 per cent in February 2012. The concerns around slowdown in the growth of these leading emerging market economies are however mitigated by the relatively positive outlook in the advanced economies.

The Committee noted that oil prices are likely to be stable in the short-to medium term, with a possibility of volatility induced by any deterioration of peace conditions in the Middle East. The risk of a sharp decline in oil price is significantly lower today than it was at the last MPC. However, there is a need to guard against complacency.

## **Domestic Economic and Financial Developments**

### **Output**

The National Bureau of Statistics (NBS) has revised the data on national accounts for 2010 and 2011. In Quarter 4 of 2011, real GDP grew by 7.68 per cent, higher than 7.30 per cent in the preceding quarter but lower than the 8.60 per cent of the corresponding quarter of 2010. For the year as a whole, real GDP growth has been lower for all the quarters in 2011 than in the corresponding quarters of 2010. The Committee noted that real non-oil GDP recorded a robust growth of 8.85 per cent in 2011 as against 8.51 per cent in 2010. Crude oil output growth recorded a decline of 0.57 per cent in 2011. In the non-oil sector, agriculture decelerated mildly: its growth was 5.71 per cent in 2011 compared with the growth of 5.82 per cent in 2010. The main contributions to non-oil growth in 2011 were wholesale and retail trade, services, building and construction, and minerals and manufacturing. In general, the negative growth in the oil and gas and slowdown in agriculture are pointers to the need for implementation of the appropriate reforms in the agricultural and petroleum sectors.

### **Prices**

The Committee noted the resurgence of inflationary threat starting in January after it had moderated towards the end of 2011. The NBS data on prices shows that the headline inflation in February 2012 stood at 11.9 per cent, lower than 12.6 per cent in January but higher than 10.3 per cent in December 2011. Food inflation on year on year basis was 12.9 per cent in February compared with 13.1 per cent in January and 11.0 per cent in December. The year-on-year core inflation was high at 13.5 per cent in February relative to 12.7 per cent in January and 10.8 per cent in December. The moderation in food inflation has helped to lower headline inflation. The rise in core inflation, however, must be kept in view in the formation

of inflationary expectations. Given the partial removal of fuel subsidy in January the moderation in inflation in February is probably attributable to a number of variables including: reallocation of spending by consumers due to higher expenditure on transport and fuel; the slowdown in monetary aggregates and fiscal spending; the stable and strengthening exchange rate of the naira; seasonal effect of food prices and statistical base effects.

### **Monetary, Credit and Financial Market Developments**

The provisional data on broad money supply (M2) for February shows that it grew by 13.4 per cent on year on year basis compared with 15.4 per cent in 2011. M1 grew at a faster pace of 19.1 per cent on year on year basis mainly owing to the strong growth of demand deposits. However, relative to December 2011 levels, both broad money (M2) and narrow money (M1) declined. Foreign assets (net) and domestic credit (net) both increased on year-on-year basis. However, over the December level, net foreign assets grew modestly by 1.15 per cent whereas the domestic credit declined by 1.9 per cent. The Committee urged the Central Bank of Nigeria to monitor closely the credit developments and ensure that the private sector gets adequate credit from deposit money banks so that the current growth momentum is not impeded by lack of adequate finance.

The Committee noted that money market rates have been moving around the upper limit of the corridor. The average OBB rate was 13.91 per cent in January and 13.64 per cent in February. The average call rates in January and February months were 14.18 per cent and 14.29 per cent, respectively. The overall stability in the money market rates was essentially a reflection of the effectiveness of monetary policy implementation. The spread between the average maximum lending rates and the weighted average rate on all categories of deposits fell marginally from 20.12 percentage points in December 2011 to 19.94 percentage points in January and further to 19.70 percentage points in February 2012.

### **External Sector Developments**

Foreign exchange reserves amounted to US\$35.43 billion as at March 14, 2012. This is an improvement over the level of US\$ 32.64 billion at end-December 2011. The exchange rate at the wDAS auctions moved from US\$/N158.6205 at the end of January 2012 to US\$/N157.6206 as on March 14, 2012. This partly reflected the moderation in the demand for foreign exchange due to increased inflows and reduced demand. The exchange rate at the inter-bank market appreciated significantly from US\$/N161.60 as at end January to US\$/N157.70 as at March 14, 2012. The rate charged by BDCs also appreciated from US\$/N163.00 to US\$/N160.00 during the same period. As a result, the premium between the wDAS

rate and the rates in the other segments of the market declined substantially over the period.

The Committee held the view that the improvement in the inflow of foreign exchange partly owing to the current high crude oil prices in the international markets and the general improvement in the policy environment to attract capital flows influenced the observed trends in the external sector. It urged the Central Bank of Nigeria to build up adequate external reserves to satisfy the genuine needs for foreign exchange consistent with the increase in the growth in economic activity and the need to conserve resources and to withstand external shocks.

### **The Committee's Considerations**

The Committee noted that the underlying inflationary pressure from supply shocks would have been more severe had there been no mitigating factors on the demand side. Currently, aggregate credit and broad money (M2) have been on the decline and there are signs of improving fiscal position with some control over expenditure and no imminent increase in wages. The fiscal stance and the absence of second-round effects of fuel subsidy removal have therefore complemented the monetary stance to dampen demand. The situation is further supported by stable exchange rates and stable international commodity prices which combine to moderate imported inflation.

The Committee recognized that in light of increasingly benign global environment, it is imperative to ensure that the current growth path is sustained. It noted the relative stability in the foreign exchange market as well as the modest accretion to external reserves during the period. In view of the poor accretion to reserves in 2011 and the need to continue to build buffers for the economy in an uncertain environment, the Committee strongly endorsed the stance of the Bank to focus on building reserves, defending the stability of the currency and providing conditions that are conducive to the inflow of FDI.

The Committee noted with satisfaction the introduction of some fiscal and structural measures that could improve the revenue base of the government as well as enhance the capacity of the domestic economy to improve the value chain in the production process. Some of these measures include introduction of cost reflective electricity tariffs and progress in agricultural transformation initiatives. Although these measures would have a salutary effect on the fiscal position, they may, in the short run, put pressure on domestic prices. Consequently, it is important for both monetary and fiscal authorities to put in place coordinated measures that would moderate the increase in the general level of domestic

prices in the short to medium term. The Committee is also concerned about the rising level of domestic debt and its sustainability, as shown by the average debt service to revenue ratio of 17.6 per cent in the last three years. This would likely have a negative impact on domestic interest rates and the flow of credit to the core private sector, among others. Although debt to GDP ratio in 2011 stood at 17.8 per cent, the Committee noted that the percentage of debt service to government revenue was a high 19.1 per cent in the same year. In view of the high interest rate environment occasioned by tight monetary policy stance, a moderation in government borrowing would be positive not just for the fiscal position but for access to finance by the private sector. After reviewing the overall fiscal position the committee commended the fiscal authorities for the discipline being introduced into government spending, the tightening of fiscal controls and the renewed focus on spending on capital projects.

In arriving at its decision, the Committee was faced with a choice between two options. One option was to consider, in view of the improving global economic environment, a moderation in headline inflation, slowdown in monetary aggregates and fiscal spending and the crowding out effects of high interest rates, a reduction in the policy rate. This argument was considered but rejected on the basis of a number of factors. These included persistent underlying core inflationary pressures, the need to continue supporting the naira and build up external reserves, the necessity for attracting and retaining foreign investment and the need for consistency and stability in the macroeconomic environment. The Bank also needs to maintain its clear focus on price stability and it is not evident that a moderation in February is sufficient to establish a trend, and warrant a reversal of monetary tightening.

#### **Decisions:**

In the light of the above, and considering the clear impact of previous tightening on the rate of inflation and exchange rates up to February 2012, the Committee unanimously decided as follows:

1. Retain MPR at 12.0 per cent with interest rate corridor of +/- 200 basis points;
2. Retain CRR at 8.0 per cent;
3. Retain minimum liquidity Ratio of 30.0 per cent; and

The Committee also resolved to watch closely developments with respect to the fiscal stance and to respond appropriately if, and when, the need arises.

#### **Sanusi Lamido Sanusi, CON**

Governor

Central Bank of Nigeria

March 20, 2012

### **Central Bank of Nigeria Communiqué No. 83 of the Monetary Policy Committee Meeting of Monday and Tuesday May 21 and 22, 2012**

The Monetary Policy Committee met on May 21 and 22, 2012 with all members in attendance. The Committee reviewed the conditions and challenges that confronted the domestic economy during the first five months of 2012, against the backdrop of international economic and financial developments; to reassess the monetary policy options in the near-to-medium term.

#### **The International Economic Situation**

The Committee noted that the global economy continued to experience sluggish recovery as the downside risks remained elevated owing to the lingering Euro zone debt crisis, weak balance sheet positions of Euro zone financial institutions, rising unemployment in most advanced economies, geo-political uncertainties affecting global oil prices and the legacy effects of the global financial crisis. Growth in the advanced economies is estimated to decelerate from 1.6 per cent in 2011 to 1.4 per cent in 2012. US output slowed from an annual rate of 3.0 per cent in Q4 2011 to 2.2 per cent in Q1 of 2012. The slow US recovery was attributed to the fall in business spending from 5.2 per cent in Q4 of 2011 to 2.1 per cent in Q1 of 2012.

In the euro area, real GDP growth is projected to contract from 1.4 per cent in 2011 to -0.3 per cent in 2012, owing to the lingering effects of the sovereign debt crisis and the attendant fragility of the financial system. Although the effects of the high commodity prices and supply disruptions from the Japanese earthquake had diminished, the effect of the Greek bailout and the failure of fiscal retrenchment have been magnified by the political impasse associated with the discussions on Greek debt exit strategy. A domino effect on other debt-ridden euro zone members and possible bank runs should not be ruled out entirely in the Euro area, if political support is not provided for the already agreed fiscal compact. European Governments are confronted with uncertainties that are coloured by both political and economic realities. The UK, Denmark and Czech Republic, with own national currencies outside the 17-nation Euro zone have been declared to be officially in recession. There are no immediate plans in the UK for abandoning austerity, and it is not yet clear if the tight fiscal stance is compatible with growth aspirations.

In the leading emerging economies, there are indications of a significant slowdown in economic activity. China has revised its growth targets for 2012 downwards, from 8.0 per cent to 7.5 per cent, compared with 9.2 per cent in 2011. Growth in Indonesia was projected to decelerate to 6.10 per cent from 6.50 per cent in 2011; while growth in Malaysia would remain unchanged at 4.40 per cent.

India's GDP growth in 2012 may not be significantly higher than the 6.50 per cent in 2011. On balance, growth in the BRICS countries is projected to decelerate as asset and currency markets reflect price fluctuations while banks and other financial institutions are under increased stress. Reflecting the slowdown in economic activities, crude oil prices in the international market have shown signs of declining as supply in 2012 is forecast to exceed demand.

In sub-Saharan Africa, inflation is trending upward while growth prospects are optimistically measured on the back of the resilience of the domestic economy in recent times. However, the new risks posed by the recession in the euro area and Chinese slowdown, in addition to the lag impact of the legacy factors associated with the financial crisis, could somewhat dampen the growth prospects. In addition, military coup d'états in some West African Countries and continuing pockets of political instability remain a source of concern.

The Committee noted the general slowdown in the global economy and the attendant softening in commodity prices which present uncertainties to the fiscal outlook, trade, and financing flows to the domestic economy, noting the very dark clouds over global economic recovery in 2012. The growing trade imbalances and threats to financial flows could weaken the external and fiscal positions.

## **Domestic Economic and Financial Developments**

### **Output**

Indications are that the robust output growth recorded in 2010 and 2011 may not be replicated in 2012. Provisional data from the National Bureau of Statistics (NBS) indicate that real gross domestic product (GDP) in Q1 grew by 6.17 per cent, down from 7.68 per cent in the fourth quarter of 2011 and 7.13 per cent in the corresponding period of 2011. This continues a disturbing and unbroken trend of decline in growth going back to Q1 2010. Overall, real GDP growth for fiscal 2012 is projected at 6.50 per cent, down from 7.45 per cent in 2011. Crude oil production was estimated to have declined by 2.32 per cent in Quarter 1, 2012 compared with a marginal increase of 0.05 per cent in the corresponding period of 2011. Non-oil real GDP growth estimated at 7.93 per cent in Q1 of 2012 was much lower than the 8.73 per cent recorded in Q1 of 2011. Growth in agriculture decelerated in Q1 to 4.15 per cent compared with the 5.54 per cent in Q1 of 2011 and 5.74 per cent in Q4 of 2011. Agricultural growth rate has not been this slow in the last seven years at least.

In general, the paradox of rising poverty incidence in the face of impressive economic growth further reinforces the Committee's call for the implementation

of the appropriate structural reforms in the key sectors notably agriculture, power and petroleum sectors, to stimulate productivity.

### Prices

As anticipated by the Committee in earlier meetings, inflationary threats re-emerged in Q1 2012, having moderated in Q4 2011. The year-on-year headline inflation which was 12.6 per cent in January 2012 moderated to 11.9 per cent in February but rose to 12.1 and 12.9 per cent in March and April 2012, respectively. Similarly, food inflation which was 13.1 per cent in January 2012 fell to 9.7 per cent in February but increased to 11.8 per cent in March before declining slightly to 11.2 per cent in April 2012. Core inflation, which declined to 11.9 per cent in February from 12.7 per cent in January, rose sharply to 15.0 per cent in March before moderating to 14.7 per cent in April 2012. On a month-on-month basis, inflationary pressure was rather benign between March and April, and the rise in year-on-year figures largely reflects the base effects in January from fuel subsidy removal. Overall inflation numbers remain within our forecast range.

The proposed upward review of electricity and import tariffs on wheat and rice as well as the rising global food and energy prices could further put upward pressure on prices in the near-term. Notwithstanding this, the lingering impact of the aggressive monetary tightening measures undertaken since 2011 and the general slow growth in monetary aggregates and the impact of rising fuel prices in consumer spending, may moderate the pressure on domestic prices in the near term. Staff projections indicate that headline inflation is projected to peak around 14.5 per cent in July 2012 before moderating steadily till the end of the year.

### Monetary, Credit and Financial Markets' Developments

Broad money supply (M2) grew by 0.01 per cent in April 2012 when compared with the level at end-December 2011. Relative to the level at end-December 2011, aggregate domestic credit (net) declined by 2.04 per cent in April 2012, translating to a decline of 6.12 per cent on annualized basis. The decline in aggregate credit during the period was mainly due to the decline in credit to the core private sector. Credit to the core private sector declined by 0.22 per cent or 0.66 on annualized basis while credit to Government (net) declined by 58.03 per cent in Q1 of 2012. Despite the decline in credit to core private sector, overall credit to the private sector rose marginally by 0.06 per cent or 0.18 per cent on annualized basis. This is indicative of a disturbing trend of growth in lending to States and Local governments at the expense of the core private sector.

Following these developments, the Committee reiterated its earlier advice that the Bank should put in place appropriate measures that would enhance the flow of



credit to the private sector, in particular to those activities that have the potential of inducing growth in a relatively short period of time.

The Committee noted that since its meeting in March 2012, money market interest rates remained anchored around the upper band of the interest rate corridor.

The interbank opened in March at 15.42 and 14.00 per cent, closed at 14.66 and 14.34 per cent, respectively, on May 17. The medium to long term yields have also eased moderately during the period. The Committee further noted a slight reduction in the spread between the deposit and lending rates. The average maximum lending rate rose to 23.31 per cent in April 2012 from 23.21 per cent in March while the consolidated deposit rate rose to 3.93 per cent from 3.79 per cent during the same period. Thus, the spread between the average maximum lending rate and the consolidated deposit rate narrowed further to 19.38 per cent in April 2012 from 19.42 per cent in March 2012.

### External Sector Developments

Foreign exchange reserves stood at US\$36.66 billion at end-April 2012, representing an increase of US\$4.02 billion or 12.32 per cent above the level of US\$32.64 billion at end-December 2011. Reserves increased to US\$38.72 billion as at 17th May 2012, representing 18.63 per cent increase over the level in December 2011. This increase reflected generally favourable commodity prices and inflows of capital in response to the removal of restrictions on repatriation and high domestic interest rates, as well as stable exchange rates. The Committees noted the assurances that total “hot money” in the system is under strict surveillance and the Bank is satisfied that the figure of US\$5 billion does not pose a threat to financial stability in view of the current level of reserves. The exchange rate at the wDAS-SPT opened at N157.62/US\$ on March 20, 2012 and closed at N157.26/US\$, on May 17, 2012 indicating an appreciation of N0.36k or 0.23 per cent. At the interbank segment, the selling rate opened at N157.70/US\$ and closed at N158.80/US\$, representing a depreciation of N1.10k or 0.7 per cent. At the BDC segment of the foreign exchange market, the selling rate opened at N160.00/US\$ and closed at N159.00/US\$, representing an appreciation of N1.00k or 0.06 per cent during the same period. The Committee noted the decline in the premia between the rates at the wDAS and the interbank and between the wDAS and the BDCs towards the end of the review period. While noting the need to put in place policies that would attract capital inflows necessary to build up adequate external reserves, the Committee urged the Bank to sustain and complement existing measures to discourage speculative demand for foreign exchange. The Committee commended the Bank for taking proactive steps to intervene in the interbank market to maintain the exchange rate within the target band.



The Committee also commended the efforts of the Bank in monitoring the foreign exchange demand and capital inflows into the economy with a view to ring fencing the economy from external shocks and other vulnerabilities; and in building the stock of reserves to meet genuine demand for foreign exchange. The Committee expressed satisfaction over the orderliness in the foreign exchange market and the stability of the exchange rate. It also encouraged the Bank to continue its close surveillance of activities in the foreign exchange market, given the current developments in the international currency and financial markets.

### **The Committee's Considerations**

The key concerns noted by the Committee were:

1. Slowdown in global economic activities, particularly, in the US, Europe and China
2. Slowdown in domestic output, especially, sharp decline in agricultural output and oil and gas sectors
3. Possible softening of crude oil prices in international markets with potential fiscal revenue loses and the likely pressure on the foreign exchange market and exchange rate
4. The inflationary threat that has re-surfaced in the first quarter of 2012, after having moderated in the fourth quarter of 2011
5. Imminent increase in electricity tariff which may lead to inflationary pressures
6. High interest rates in the face of declining GDP output; and
7. Security concerns in the country
8. Slow pace of structural reforms induced by failure to improve power supply, establish and implement reliable PPP framework that can attract funding for infrastructure, and delay in passing the PIB

The Committee noted that since its meeting in March 2012, the uncertainty surrounding the global economy remained elevated owing to continued economic slowdown in advanced and major emerging economies as well as the financial stress in key advanced economies. These developments will impact the domestic economy through the trade and financial flow channels, weakening the external and fiscal positions. Monetary policy on its own has limitations with respect to inducing long-term growth which is dependent on fiscal and structural measures relating to petroleum, power and infrastructure sectors. This Committee reiterates the need to recognize the short-term nature and limits of monetary policy. The growth and development of the Nigerian economy will continue to be at risk so long as progress is not made in structural reforms.

Furthermore, the Committee reassessed the recently released provisional output data which indicated a slowdown in GDP growth. It noted that the huge drop in

agricultural output was traced to the following factors: displacement of farmers in the northern part of the country owing to security situation, inadequate rainfall and increased production cost due to the partial removal of fuel subsidy in January 2011. It also noted the decline in oil and gas production and the recent revelation by the oil Minister of the loss of over US\$7 billion of revenues due to oil theft. It concluded that the interest rate movements will not be effective in stimulating growth under such circumstance and urged government to fast-track the agricultural transformation initiative and to strengthen fiscal controls over the oil industry.

The Committee also noted that while the lingering impact of the aggressive monetary tightening measures undertaken since 2011 served to moderate the pressure on domestic prices in the near term, the effect of the global economic and financial developments on exchange rate and domestic prices could be significant in the coming months. The international oil price output and the lag in oil supplies in relation to demand seemed to indicate the onset of additional pressures on foreign exchange reserves, exchange rates and prices. These developments require that the power and petroleum sector reforms as well as infrastructure investments need to be scaled up as quickly as possible. These should complement measures to enhance credit flows to the private sector, in particular to growth inducing activities, so that the likely pressures on interest rates are addressed.

The Committee welcomed the efforts being made to improve fiscal consolidation. Government revenues have improved in Q1 in relation to government expenditures, resulting in notional fiscal surplus. The Committee encourages that these efforts are furthered, especially in view of the growing domestic public debt stock. The Committee also noted the very healthy collaboration that has been established between the fiscal and monetary authorities and urged the Bank to continue supporting the fiscal authorities in their pursuit of very difficult reforms.

The Committee evaluated the policy options available to it and the analysis of alternative scenarios and agreed that monetary policy should contribute to the consolidation of a positive and stable longer-term macroeconomic environment conducive for growth and development. It was in the Committee's view that at this point in time, the trajectory of prices and output is dependent on fiscal and structural policies than on the monetary stance. The sluggish growth in credit, stable exchange rate, healthy reserve position and benign month-on-month inflation do not suggest a need for further tightening at this point. Also, the underlying reasons for slowdown for agric and oil GDP growth will not be addressed by monetary easing.

### **Decision**

The Committee, therefore, decided by a unanimous vote to maintain the current stance of monetary policy without discounting the possibility of changing it, should economic and financial conditions warrant so in the near term. As such, the Monetary Policy Rate (MPR) is retained at 12.0 per cent with the symmetric band at +/- 200 basis points. The Cash Reserve Ratio (CRR) and Liquidity Ratio (LR) also remain unchanged.

### **Sanusi Lamido Sanusi, CON**

Governor  
Central Bank of Nigeria

*May 22, 2012*