MINUTES OF THE 218TH MEETING OF THE MONETARY POLICY COMMITTEE (MPC) HELD ON MONDAY 24TH AND TUESDAY 25TH JANUARY, 2011 IN THE MPC MEETING ROOM, 11TH FLOOR, CBN, ABUJA

ATTENDANCE

1. Sanusi L. Sanusi	-	Governor, (Chairman)
2. Tunde Lemo	-	Deputy Governor, Member
3. Sarah O. Alade	-	Deputy Governor, Member
4. Suleiman Barau	-	Deputy Governor, Member
5. Kingsley Moghalu	-	Deputy Governor, Member
6. Sam O. Olofin	-	Board Director, Member
7. Adedoyin R. Salami	-	Member
8. Abdul-Ganiyu Garba	-	Member
9. John Oshilaja	-	Member
10. Chibuike U. Uche	-	Member
11. Shehu Yahaya	-	Member,
12. Danladi Kifasi	-	Member, Perm. Sec. Fed. Ministry of Finance
13. Okorie A. Uchendu	-	Director, MPD, Secretary
14. Christopher M. Okafor	-	Dep. Director, Dep. Sec

OBSERVERS

1. Rasaki A. Sanusi	-	Ag. Stat. General, NBS
2. Sam O. Oni	-	Director, Bank. Supervision
3. Charles N. O. Mordi	-	Director, Research
4. Sani I. Doguwa	-	Director, Statistics
5. Joe Alegieuno	-	Director, Dev. Finance
6. O. F. Owolabi	-	Ag. Director, Fin. Markets
7. Folakemi Fatogbe	-	Ag. Director, Risk Mgt
8. Nathaniel T. Igba	–	Dep. Director, Trade & Exch
9. Festus C. Agu	-	Dep. Director, Reserve Mgt.

Day 1:

Opening

1.) The meeting commenced at 10.02 a. m. with a prayer by Abdul Ganiyu-Garba. In his opening remarks, the Chairman welcomed members to the first meeting of the year and informed them of the intention to publish the names and attendance of members in this year's Annual Report and Statement of Accounts of the Central Bank of Nigeria (CBN). He also announced that the press conference would hold at 2.30 p.m. instead of the usual time of 3.00 p.m. To that effect, the Deputy Governor, Economic Policy (DG (EP) suggested that the following day's meeting should commence at 9.00 a.m. to facilitate an early production of the communiqué.

Minutes of the Previous Meeting

2.) In reviewing the minutes of the 217th meeting of the MPC held during November 22 - 23, 2010, members felt that the entire section on matters arising should be re-written to reflect the actual concerns expressed by members. The following specific observations were also made:

Page 3: last line, "attended" should be replaced with "attend".

Page 6: line 3 from bottom should read "credit classified as sub-standard" instead of "standard".

Page 28: line 10 from bottom should read, "Application for Guarantee Certificate to the tune of N107.5 million, made up of N100.0 million to First Bank of Nigeria and N7.5 million to the National Economic Reconstruction Fund (NERFUND) had been approved under the SME Credit Guarantee Scheme, as at end-November, 2010".

Page 34: The Chairman observed that in an attempt to be precise, the minutes were robbed of the robust discussions held during the meeting. It was also pointed out that the decision reached was a "majority decision" and not a "unanimous decision" as reported.

Matters Arising from the Minutes of the Last Meeting

3.) The Chairman pointed out that the Asset Management Corporation of Nigeria (AMCON) had actually purchased some of the banks' toxic assets, and that about N770 billion worth of bonds had been issued in respect of the non-performing loans (NPLs). He, however, cautioned that as more money go into the recapitalization of banks, liquidity pressures might arise in the banking system.

A member noted that the structure of the minutes was such that a greater proportion of it was devoted to the banking system presentation, which was unusual for minutes of a Monetary Policy Committee. Such minutes, he said, should focus more on monetary policy issues. It was also observed that substantial portions of the background paper presentations at the MPC found their way into the minutes, whereas a summary of their relevant sections would suffice. In essence, the minutes were expected to focus more on capturing the discussions of the presentations and the underlying arguments, rather than the details of the papers presented.

A member observed that the minutes of the 216th MPC meeting had been posted on the Bank's website in line with the decision reached at that meeting. Members welcomed the development and the Chairman directed that the approved minutes should be posted on the Bank's website within two weeks of each MPC meeting, after it had been vetted by the DG (EP) and two volunteers that are not members of the Committee of Governors (COG). In that regard, the DG (EP) suggested that instead of having a committee of three, the minutes should be sent to members and their comments returned promptly. The Chairman then concluded that members must take responsibility for going through the minutes. The whole idea of posting the minutes on the website was to make for openness and provide the public with more information on how the major decisions reached at the MPC were arrived at. In the same vein, the Chairman stated that the minutes should contain a short note of about one paragraph from every member, supporting his or her vote during the MPC meeting. The MPC secretariat was mandated to collate the notes.

Presentation by the Monetary Policy Department:

4.0 Economic Report and Proposals for Monetary Policy Actions

The Economic Report covered developments in both the domestic and international economies, and outlook for the near-term.

Domestic Economic Developments

On the domestic economy, the focus was on developments in output, prices, fiscal, external sector and financial markets.

The presentation indicated the following output and price developments:

i) Projections by the National Bureau of Statistics indicated that real Gross Domestic Product (GDP) grew by 7.85 per cent in 2010 compared with the revised figure of 6.69 per cent in 2009.

ii) The non-oil sector was projected to grow by 8.92 per cent in 2010 compared to 8.61 per cent in 2009, largely driven by the agriculture, wholesale/retail trade and services sectors with relative contributions of 2.39, 2.04 and 2.08 per cent, respectively.

The oil sector was projected to positively contribute 0.05 percentage point in the third quarter and 0.04 percentage point in the fourth quarter of 2010

iii) The year-on-year headline inflation decreased to 11.8 per cent in December, 2010 from 12.8 per cent in November 2010, and 13.6 per cent in September, 2010. Of the December inflation rate, food inflation contributed 6.46 per cent.

Similarly, core inflation declined to 10.9 per cent in December, 2010 from 11.7 per cent in November, 2010. Food inflation also dropped to 12.7 per cent in December, 2010 from 14.4 per cent in November, 2010.

In terms of financial market developments, the report indicated that:

iv) At the inter-bank market, the call and OBB rates rose to averages of 8.45 and 7.43 per cent, respectively, in October 2010, in response to the upward review of the MPR and IT challenges experienced in September, 2010. The rates, however, moderated to 8.06 and 6.86 per cent in December 2010, while MPR remained at 6.25 per cent.

v) The average maximum lending rate decline from 22.20 in September, 2010 to 21.84 per cent in November 2010. The average prime lending rate also fell from 16.66 in September to 16.11 per cent November, 2010.

vi) The weighted average savings rate declined consistently from 3.2 and 1.95 per cent in March and June, 2010 to 1.49 and 1.48 per cent in September and November, 2010, respectively. The consolidated deposit rate which declined from 2.09 per cent in June to 2.07 per cent in September rose to 2.36 per cent in November, 2010.

Thus, the spread between the average maximum lending rate and the consolidated deposit rate widened from 19.94 per cent in June to 20.14 per cent September, before narrowing to 19.48 per cent in November, 2010.

vii) At the foreign exchange market, total demand and sales in 2010 amounted to US$29,785.70 million and US$25,167.81 million, respectively, which were equivalent to an average of US$307.10 million and US$259.46 million per auction, respectively. This compared with the total demand and sales of US$35,471.13 million and US$24,204.80 million recorded in 2009. The sales/ demand ratio per auction rose from 80.4 per cent in September to 91.0 per cent and December, 2010. On the average, 84.11 per cent of foreign exchange demand was met in 2010.

In December, 2010, the wDAS exchange rate recorded a depreciation of N0.26 or 0.17 per cent compared to the preceding month. In the BDC segment, the market recorded a depreciation of N1.44 or 0.94 per cent. Similarly, at the inter-bank market, the average selling rates in December, 2010 indicated a depreciation of 0.22 per cent from that recorded in November, 2010.

viii) The country's gross external reserves stood at US$32.34 billion at end-December 2010, indicating a decline of US$2.16 billion or 6.3 per cent compared with US$34.50 billion at the end of September 2010. The reserve level fell by US$11.04 billion or 25.45 per cent when compared with US$43.38 billion as at end-December, 2009. However, as at January 20, 2011, the external reserves stood at US$33.26 billion, representing an increase of US$0.92 billion or 2.84 per cent when compared with end-December level.

The report also indicated that, total foreign exchange inflows from January to December, 2010 was US$27,877.04 million, representing an increase of US$2840.77 million or 11.35 per cent over the $25,036.27 million recorded in the corresponding period of 2009. Of this inflow, crude oil/gas revenue was US$26,166.69 million or 93.86 per cent. Total

	outflows for the same period amounted to US$37,923.57 million. The CBN funding of the foreign exchange market accounted for US$24, 836.27 million or 65.49 per cent of the outflows. Thus, there was a net outflow amounting to US$10,046.53 million in 2010 compared with $10,484.83 recorded in the corresponding period of 2009 ix) On the fiscal side, total federally-collected revenue for the period January – November 2010 stood at N5,725.76 billion, of which oil revenue accounted for N4,857.40 billion or 84.83 per cent. The amount collected was lower by N772.62 billion or 11.89 per cent relative to the proportionate budget estimate of N6, 498.38 billion. The overall fiscal operations of the Federal Government for the period (January to November, 2010) resulted in a deficit of N1, 529.33 billion. The deficit was financed through DMO borrowing from the domestic market (N893.79 billion), FGN Share of Excess Crude Account (N199.54 billion), Privatisation Proceeds (N6.36 billion), World Bank Loan (N75.03 billion) and Loans from Special Accounts (N337.56 billion) x) The monetary analysis indicated that broad money supply (M2) increased by 6.7 per cent in December, 2010 (on an annualized basis) compared with the indicative benchmark of 29.26 per cent for 2010. Net aggregate credit to the economy grew by 13.4 per cent, on an annualized basis, in December, 2010, compared to 59.6 per cent recorded in December, 2009. This was driven mainly by the substantial credit to the Government which grew by 67.83 per cent, while credit to the private sector fell by 4.92 per cent (annualized) in December 2010 as against the benchmark of 31.54 per cent for 2010.	

Reserve Money continued to remain below the indicative benchmark in most periods of 2010. As at January 10, 2011, the RM stood at N1, 535.67 billion below the 2011 Q1 provisional indicative benchmark of N1,784.94 billion by N249.27 billion or 13.97 per cent

xi) Demand for the Standing Lending Facility (SLF) decreased from N1,356.16 billion in November to N859.61 billion in December, 2010. However, patronage of the Standing Deposit Facility (SDF) rose from N443.71 billion in November to N1,099.28 billion in December, 2010.

xii) Nigerian capital market indicators recorded significant improvements during the year 2010. The All Share Index (ASI) increased by 18.93 per cent from 20,827.17 as at end-December, 2009 to 24,770.52 at end- December, 2010. Similarly, market capitalisation increased by an annualized growth of 58.83 per cent from N4.98 trillion as at end-December, 2009 to N7.91 trillion at end-December, 2010.

Developments in the Global Economy:

xiii) The report noted that the performance of the global economy was mixed. In general, there were continuing signs of global economic recovery as more countries reported signs of rising output, moderating inflation, improving stock market indices and moderating exchange rate depreciation.

Monetary policy rates in most countries across the world were reduced or kept low during 2010, in an attempt to enhance liquidity to sustain recovery and growth. Monetary policy innovations using quantitative easing were also adopted to pull some economies out of recession.

Despite these developments, the report emphasized the need to monitor developments in the Euro area economies, particularly the PIGS - Portugal, Italy, Greece, and Spain because of the potential adverse impact of recent developments in these economies. Other developments included: political upheavals in North Africa, especially in Tunisia and Algeria; flooding in Australia, Bangladesh and Sri Lanka with implications for food prices and security; and election stalemate in Ivory Coast with its possible adverse effects on the economies in the West African sub-region.

Outlook for the Near-term

In terms of near-term outlook, the report indicated that real GDP growth in 2011 could be higher than in the preceding year based on the following assumptions:

- Resolution of the Niger Delta crisis and government's amnesty programme for militants;
- Improved oil prices and output;
- Prospects of high agricultural output;
- Impact of banking sector reforms and the intervention funds;
- Stability in the supply and prices of petroleum products; and
- Expected improvement in electricity supply.

With regard to prices, staff projections indicated that the year-on-year headline inflation would fluctuate between 11.1 and 12.3 percent in the next six months.

xiv) Similarly, money market rates were not likely to moderate in the light of government borrowing.

Staff forecasts indicate that if the current exchange rate policy stance of liberalizing the foreign exchange market, with a view to enhancing foreign exchange supply was sustained, the exchange rate would likely remain stable in the near-term.

Federal Government expenditure was expected to increase in the first quarter of 2011 due to election expenses and concurrent implementation of 2010 and 2011 budgets.

Forward prices of oil posted on the New York Mercantile Exchange suggested that crude oil prices would rise during the rest of the year and beyond.

xv) A summary of the business expectations survey conducted by Brickfield Road Associates (BRA) Limited indicated that:

- All the sectors surveyed expected an improvement in the economy.
- Employment was expected to rise but manufacturing sector was anticipated to remain unchanged
- Inflation was generally expected to rise in the next three months
- Interest rate was generally expected to rise in the next three months
- Appreciation in the naira exchange rate was expected in the next three months. However, some sectors expected some level of depreciation in the next six months.
- Input Cost was expected to rise
- Most sectors expected output to rise
- MPR was expected to remain unchanged for the next three months. However, it was expected to be increased in the next six months

xvi) Based on the review of economic developments and outlook for the near term, the report identified the following pressure points and policy challenges:

Pressure Points:

- Persisting fluctuations in the interbank call and OBB rates
- Tight credit conditions and high lending rates
- Expected high government expenditure in the first quarter of 2011
- Depreciating naira exchange rate in the face of declining stock of external reserves

Challenges for monetary and credit policy in the next two quarters included:

- providing adequate liquidity and easing credit conditions in the market;
- locking-in on lowering inflation expectation;
- Domestic financing of Federal Government fiscal deficit; and
- Moderating the declining stock of external reserves.

Thus, the key thrust of Monetary Policy in 2011 were identified as:

- Focus on maintenance of price stability;
- Sustenance of monetary tightening to address the emerging signs of inflationary threat;
- Maintaining market-driven interest rates
- Achieving stable naira exchange rate
- Sustenance of output growth
- Ensuring a safe, sound and stable banking system

<u>Proposals for Monetary Policy Actions</u>

In view of the foregoing, the following policy proposals were presented for the consideration of the MPC:

<u>Scenario 1:</u>

- **The MPC may retain the MPR at 6.25 per cent and the current interest rate corridor**

Pros:

- Maintaining the current monetary policy stance would sustain market expectations at the current level with respect to inflation, interest and exchange rates.
- There would be no interruption of the current policy measures which would facilitate the achievement of their objectives.

Cons:

- It might signal non-recognition of inflation threats arising from anticipated liquidity injections from election expenses, CBN quantitative easing policy and government expenditure, especially the concurrent implementation of 2010 and 2011 budgets in the first quarter of 2011.

Scenario 2.

(a) The MPR should be raised by 25 basis points to 6.50 per cent and the current interest rate corridor be retained;
(b) Raise the liquidity ratio from 25.0 per cent to 30.0 per cent effective March 1, 2011;
(c) Increase the cash reserve ratio from 1.0 per cent to 2.0 per cent effective January 31, 2011.
A selection of (a) to (c) or a combination of any of the three may be considered

Pros:

- This would signal monetary policy tightening in response to the prospects of inflationary pressures from anticipated liquidity injections from CBN quantitative easing, election expenses, AMCON and Government injections.

Cons:

- Raising MPR, CRR and Liquidity ratio could further increase lending interest rates and slow down the current policy efforts at channelling credit to the real economy.

Scenario 3.

- **The MPR should be reduced by 25 basis points with the current interest rate corridor retained.**

Pros:

- This would signal monetary policy easing in order to further spur economic growth and employment generation

Cons:

- Lowering MPR could risk the current moderation in the downward inflationary trend.

Discussion of the Report

In discussing the report members felt that the outlook for 2011 presented in the report was too optimistic. It was noted that there was likely to be increased spending in the run up to the elections in April 2011, so the risk of inflation would be on the upward side. Other factors that might cause inflation to trend upward were, increasing global food and energy prices, as well as spending by AMCON.

Concerning the capital market, the sentiment was that it was in a recovery mood. Going by recent criticisms, a member wondered if the Bank had not abandoned its inflation objective given the consistent focus on financial stability. The Chairman

	drew the attention of members to the Banks’ reform document which clearly stated that the Bank would pursue a hybrid monetary policy that targets inflation and financial stability. On the depletion of the external reserves, members felt that the structural problem of our economy as an import- dependent country was partly responsible for the depletion of the reserves. The depletion of the reserves should be explained in terms of how much was spent on JVC cash calls, subsidies on petroleum products and funding of the WDAS, among others. The public needed to be informed that if we did not expend the reserves, we probably would have had to borrow. Also, the point should be made that we perhaps would not have had inflation moderating if we had not expended the reserves to stabilize the exchange rate. However, it was emphasized that the expenditure on JVC cash calls needed to be made transparent. In that regard, the Extractive Industry Transparency Initiative needed to be revived. It was restated that the depletion of reserves could only be substantially addressed by attending to the fundamental structural problems of the economy. It was presumed inconsistent to preserve reserves simply as an end by itself, in a highly import-dependent economy. It would imply deliberately starving the	

economy of essential imports where there are no import competing substitutes. Specifically, whenever we are able to get the refineries working again, and import of petroleum products considerably reduced, and whenever we are able to boost the production of our import-competing goods, especially food items such as rice, and significantly reducing their imports, we would be back in a strong position that enhances our capacity to conserve and build our foreign reserves. However, given the expectation for improved oil output and prices, the MPC was looking forward to the rebuilding of the external reserves and excess crude account that were depleted in 2010.

Members welcomed the trend whereby inflation was seen to be declining, but wanted to know the major drivers of the decline.

On savings, members expressed concern about the low savings rate which had declined to about 1.0 per cent. From an economic perspective, and for financial inclusion, it was important to consider small savers by rewarding them reasonably and fairly. They emphasized that if that was not addressed, the banks would face the problem of disintermediation when the CBN guarantee of interbank transactions was eventually removed. There was, therefore, the need to set a minimum savings deposit rate, as was the practice in most developing countries. Accordingly, the Committee mandated Dr. Vasudevan Asuri and BSD to conduct a research on minimum savings/deposit rates across countries, as a basis for drawing up policy guidelines on the issue.

On capital market analysis, the Committee suggested the need to determine the peaks of market capitalization of the Nigerian Stock Exchange (NSE) in 2007/ 2008 and to see how the market had recovered in 2010 when viewed against the peak. The Committee, however, noted the general reduction in the share of the banking sector in the capital market from about 70 per cent during its peak to about 36 per cent.

The MPC also sought to know how much foreign exchange was sold by CBN to Class "A" BDCs in 2010.

Notwithstanding the economic developments cited above, it was pointed out that there were heightened political risks associated with the build up to the elections and the need to pay attention to security, especially in the volatile regions. It was emphasized that part of the political risk was the failure of policies to provide jobs to stem unemployment. After an exhaustive deliberation of the economic report the Committee agreed that the policy thrust would be to sustain monetary tightening in 2011.

At the end of the discussions, the Chairman provided the summary of the key issues, to enable members have a clear direction in preparation for the decisions during the next meeting day. The summary was as follows:

(i) Although inflation had moderated for two consecutive months, its outlook, however, pointed to an upward risk because of inflation pass through to the domestic economy, since the country imports petroleum products. There were also increased expenses associated with AMCON, and election spending, all of which would put upward pressure on inflation.

(ii) He observed that foreign reserves were beginning to show signs of stabilization.

(iii) He re-emphasized the Committee’s commitment to price stability, and in 2011, hoped to see progress on various reform measures that should attract foreign investment and help in moderating the structural problems of the economy. The government was commended for its efforts at reducing overhead expenditure.

(iv) He further observed that the recovery noticed in the capital market was progressing satisfactorily.

(v) The greatest challenge facing the economy he identified was the lack of flow of funds into critical sectors, a development which called for the need to unlock the flow of credit into critical investments in agriculture, SMEs and manufacturing sectors.

(vi) On the government side, there was the need to enunciate the right policies, as well as create the regulatory and institutional environment, including continued fight against corruption and provision of adequate infrastructure.

(vii) On the Bank's side, the CBN would continue to engage the banks in reforms/intervention to channel credit to the critical sectors.

After the summary, the MPC through Prof. Sam Olofin congratulated the Governor for being conferred with the Man-of- the Year award by the *Nigerian Tribune* Newspapers, among other awards. The Chairman thanked members for the support and restated that he dedicated the awards to the hardworking staff of the Bank as well as other stakeholders including the

Presidency, National Assembly, the Police and EFCC, who made whatever achievement that was recognized, possible.

CLOSING: The meeting rose at 5.59 pm with a prayer by Dr. Sanni Doguwa.

DAY 2, 25th January, 2011

The meeting commenced with a prayer by Tunde Lemo, Deputy Governor, Operations.

The Chairman did a recap of issues discussed at the previous day's meeting stressing that the easing mode in monetary policy action had been exited. He, however, remarked that the challenge facing the Committee was to decide on whether to maintain the status quo as at the last MPC or further tighten monetary policy, and if so, the instruments to be used. He argued that inflation had been trending downward since November, 2010 and that could be one of the arguments for not doing anything. However, he remarked that with the deregulation of the power sector and rise in crude oil prices, with possible reduction in subsidy or increase in government borrowing/spending, there was bound to be inflationary threats and erosion of reserves. Again, from two months thence, AMCON was expected to have recapitalised all banks and that would have implications for system liquidity. The Chairman further observed that Nigeria lost about US$10.0 billion in reserves in 2009 and 2010, respectively and that if the trend persisted in 2011, the country will either lose its reserves or face exchange rate depreciation, which was counter to the policy stance of exchange rate stability. More importantly, he noted that the continued demand for foreign exchange (and consequent depletion of reserves) was a reflection of the import-dependent nature of our economy. There was, however, the need to sustain the observed increase in external reserves. The above arguments, did not suggest the need for a more accommodating monetary policy stance. Rather, the policy choice was clearly whether to continue with the last MPC position or tighten monetary policy.

Having provided a synopsis of the policy choices and the arguments for and against each option, the next decision was on the instruments that would be employed. A combination of the Monetary Policy Rate (MPR), Cash Reserve Requirement (CRR) and Liquidity Ratio (LR) were suggested. Nevertheless, it was acknowledged that the effectiveness of the above measures could be limited by the existing structural problems in the economy.

<u>Individual Positions and Arguments for the Policy Choices</u>

Having analyzed the issues, the Chairman invited members in turn to make their policy choices and justifications known.

<u>John Oshilaja:</u>

He agreed with the Chairman’s position that monetary easing was no option. He, however, argued that the issue of whether the MPC continued with monetary tightening was a more difficult one as we have not seen the inflation drivers working. He, therefore, supported the maintenance of the previous position.

<u>Adedoyin R. Salami:</u>

He observed that the stance of the MPC at its previous meeting was to leave MPR unchanged and watch the outcome of events. Although he noted that there were some issues around the instruments to be used and also doubted whether low inflation was sustainable, he expressed the need for caution and, therefore, supported the maintenance of the previous position.

<u>Chibuike U. Uche</u>

He held the position that the status quo should be maintained as we were in the middle of a banking reform and would want banking stability. He further stressed that a major objective of monetary policy was to promote real sector growth and that inflation was only anticipated, while available statistics

	showed that it had not happened, but was actually trending down. He noted that a positive development as contained in the Chairman’s statement was that the President himself was leading the campaign for prudent spending and economic management. He, therefore, did not think that the benefits of taking a proactive action would outweigh the costs, hence he supported that the status quo be maintained. <u>Shehu Yahaya:</u> In contrast to the previous speakers he argued for monetary tightening. The argument was predicated on the tangible prospects for higher fuel prices, increased spending due to the impending elections, and additional injection of liquidity from AMCON activities. These factors may provoke inflationary pressures and Naira depreciation, which in turn may stroke further inflation and deplete the reserves. <u>Tunde Lemo:</u> Tunde Lemo argued that the Committee could ill-afford to ignore the increased spending that would arise as a result of the fact that we are in an election year. The negative real interest rate and the risk of financial disintermediation as a result of higher inflation were worrisome, if interest rate was not adjusted upward. He, therefore, favoured monetary tightening.	

Sarah Alade:

In her submissions, she argued that the declining inflation was not sustainable and that we were losing reserves fast. If monetary policy was not tightened, then pressure from that window would make us to continue to lose reserves and that would have serious implications for the economy. She went further to argue that although there was no information on inflation expectation, the threat of higher inflation was real and would be exacerbated with election spending. She, therefore, supported monetary tightening.

Kingsley Moghalu:

Kingsley Moghalu argued that although inflation was slightly reduced, it was not sustainable and that the reasons already adduced for the need to shore up reserves were quite compelling. He warned that if the Committee did not agree to tighten monetary policy then, it might be too late by the next MPC that would hold in March, 2011. He, therefore, favoured monetary tightening.

Suleiman Barau:

He supported the tightening of monetary policy and observed that it was consistent with the Committee's position during the last MPC meeting. He saw no reasons for a change to that position as the compelling reasons included the need to ensure stability in the foreign exchange market and tame the upsurge in liquidity.

Sam O. Olofin:

He argued that given the anticipated liquidity upsurge and de-accumulation of foreign reserves, as well as information available from other indicators, the Committee should have started the process of tightening much earlier. He emphasised that the MPC should not allow the emergence of spikes but rather a smooth adjustment process in their monetary policy actions. He noted that it was better for the MPC to have incremental measures and also pay attention to impact lag of monetary policy. He, therefore, favoured monetary policy tightening.

Abdul-Ganiyu Garba:

Having listened to previous arguments, he remarked that majority of members seemed to support the policy on monetary tightening which was the decision taken at the last MPC meeting in November but the argument remained which instruments to apply. However, he suggested that in subsequent meetings, the Committee should spend more time observing the behaviour of the high frequency data, pre and post MPC meetings. Such observations and analysis would help the Committee determine what happened before and after the decisions at the MPC meetings. He observed that even though inflation appeared to be trending down, he was concerned about the dwindling reserves. He further observed that the biggest threat to inflation was the value of the naira and that if the naira depreciated there would be mark up in prices. He, therefore, voted for tightening, which was consistent with the position at the last MPC, but remarked that the choice of instruments was key to the outcome of the decisions.

Danladi Kifasi:

Danladi Kifasi remarked that having listened to the brilliant arguments of the earlier speakers, he was inclined to align himself with the majority opinion. However, he was worried about the possible impact of monetary tightening on the treasury. He argued that if the Committee strengthened the naira so much, then the government would have problem with its revenue when they monetize the dollar proceeds, and that would affect government projects. Thereafter, he voted for monetary policy tightening.

Sanusi Lamido Sanusi:

In his submissions, the Chairman stressed that the greatest threat to inflation was the anticipated liquidity pressure and that a lot of what was done and achieved by the MPC relied on credibility of the authorities. He argued that if the Bank had made a commitment to exchange rate stability, there was a cost in moving away from that position. Consequently, if the Committee felt that the observed inflation level was not sustainable, then they must find an intelligent way to adjust. He emphasised that it was difficult to justify exchange rate depreciation where prices were high and the country was an import-dependent economy. The only argument for it was that government wants more money. Since part of the objectives of monetary policy was exchange rate stability, it was better to prevent the depreciation of the naira, rather than give government more money and for it to have less to spend in real terms. He went further to argue that the demand for foreign exchange was actually driven by banking system liquidity and that the only way to keep the naira exchange rate within an acceptable band, with the influx of liquidity anticipated from AMCON, election and all that, was to tighten monetary policy.

He also observed that the uncertainty surrounding the elections was a big issue as foreign investors were waiting to see what would happen after elections, while the local investors were thinking of where to take their money to if problems emerge as a result of the outcome of the elections. He, therefore, asserted that the immediate reasons for monetary policy tightening were to preserve the external reserves level and ensure exchange rate stability. He pointed to clear indications that a moderation in inflation was almost an aberration. Continuing, he alluded to the global increase in energy and food prices and Nigeria's vulnerability as an import dependent nation that also imported oil. He argued that if oil prices went up, that would translate to more subsidies to the Nigerian National Petroleum Corporation (NNPC) for imported petroleum products. He reminded members that he voted for a hold on monetary policy action at the last MPC meeting, but observed that the situation was quite different, given an inflation rate of 11.8 per cent in December, 2010. He observed that the MPC did quantitative easing to save our ailing economy and that the justification for further monetary accommodation gets weaker, even as the capital market was recovering and oil prices were rising. He, therefore, voted for monetary policy tightening.

At that juncture, he enquired to know whether any of the members that were not formally in favour of tightening had changed their minds after listening to the arguments. Based on that, the following discourse ensued.

John Oshilaja:

John Oshilaja remarked that he generally supported tightening, but his problem was whether the timing was right. His other concern was for the flexibility the Committee might lack in the future, if it used up all the instruments at its disposal then.

Sanusi Lamido Sanusi:

The Chairman reminded him that the MPC had actually moved MPR up by 25 basis points in 18 months. He, therefore, remarked that an MPR of 6.25 per cent was actually very far from the pre-crisis position. He also said that the CBN had been very active in the Open Market Operations (OMO) and would prefer the Bank relied more on that.

John Oshilaja:

Having accepted the above arguments, he changed his vote in favour of tightening, but proposed that the action should take the form of a gentle process.

Adedoyin R. Salami:

Having listened to various shades of arguments and made the point about negative interest rate, he agreed on balance to monetary tightening as the movements in MPR and inflation rate were both critical for inflation management. He was further compelled to change his mind as he was not convinced that the fiscal authorities would exercise restraint in spending as we moved closer to the elections.

Sanusi Lamido Sanusi:

In response, the Chairman drew his attention to the outcome of the fiscal analysis which showed that recurrent expenditure constituted over 70.0 per cent

	of 2010 budget expenditure. He observed that that was a sure signal for inflation. Furthermore, the fiscal authorities had always out-performed the target for recurrent expenditure which was also expected to hit the market faster. <u>Danladi Kifasi:</u> He acknowledged the point made by the Chairman but remarked that a lot of the recurrent expenditure had gone to maintenance and payment of salaries. Although he agreed to tightening, he still had his reservations as government was bound to be constrained by that decision. <u>Sam O. Olofin:</u> In his contributions, he opined that the views of MPC members were not in any way contradictory as they were meant to complement fiscal measures. He argued that if government received a larger quantity of naira and bought less with it that would have amounted to money illusion. He, therefore, concluded that a weaker naira was not even in the best interest of fiscal authorities. <u>Danladi Kifasi:</u> In his final submission, he ended rhetorically by posing the question, how do we then ensure that Banks lend to the private sector? <u>Chibuike U. Uche:</u> Chibuike Uche maintained his position in favour of	

the status quo, arguing that exchange rate stability was not sustainable in the long-run. He observed that if monetary policy was tightened at that point, interest rate would go up and was, therefore not convinced the MPC should tighten monetary policy stance at that stage when inflation was coming down.

Sanusi Lamido Sanusi:

Reacting to the issues raised, the Chairman observed that he was very passionate about the real sector but that the long-term solution lay in structural reforms in the economy. He stated that monetary policy had its limitations in terms of the control of credit to the real economy. The critical issue was that of access to credit as lenders tend to gravitate to big borrowers. That, he said, was really the challenge. He stated that addressing the flow of credit to the real sector required extra action outside of monetary policy. He directed that the communiqué should stress those points made, if we want to address the problem of attrition of reserves.

The Chairman remarked that cheap money usually led to bubbles either in the money or foreign exchange market, and that the bubble was likely to appear in the foreign exchange market. **Having said that, he announced a vote of 11: 1 in favour of monetary policy tightening.**

Nature of Monetary Policy tightening and the Instruments to be Used

On the nature of monetary policy tightening and the instruments to be used, a second round of discussions and voting by MPC members was conducted to determine whether the tightening should be gradual, symbolic or significant in terms of process and magnitude. A related argument was the nature of instruments to be deployed. The decisions were guided by the need to send clear signals to the market that the CBN was willing and ready to intervene in the market at anytime it deemed fit. They noted that the most critical risk was excess liquidity in an environment of political uncertainty and that those issues posed challenges to inflation and exchange rate stability. The issue of timing was seriously considered as time was of essence in taking monetary policy decisions. The instruments considered were the MPR, the Liquidity Ratio (LR) and the Cash Reserve Requirement (CRR). The LR was found to be above 20 per cent for most banks while the CRR was considered the most effective way of dealing with system liquidity because of its instantaneous effect. Those who had contrary views were also asked to air them, as some had lingering concerns about the probability of the anticipated inflationary pressures manifesting. In that regard, they did not favour the deployment of a suit of measures when the magnitudes of their likely effects were not very clear.

Summary of the Results of the Second Round of Voting

The Chairman summarised the results thus:

By a ratio of 11:1 the MPC members voted to tighten monetary policy stance, based on reasons already outlined above. The member who voted against tightening wanted rates to remain where they were in view of the fact that inflation was moderating and also to avoid the risk of elevated lending rate for borrowers. The Chairman stated that it was time to begin to return and retrace our footsteps until we gradually return to normalcy. This implied that the 2009 posture was being gradually unwound as banks return to normalcy.

He also stated that by a decision of 11:1 members decided to increase MPR by 25 basis points. However, by a vote of 7:4:1 members voted to leave the symmetric corridor around the rate. Four (4) of the voters wanted the SDF increased by 50 basis points, while one (1) member wanted the status quo maintained.

Again, by a ratio of 11:1, members voted to:

(i) increase the LR from 25 to 30 per cent with effect from March 1, 2011; and

(ii) increase the CRR from 1 per cent to 2 per cent with effect from February 1, 2011.

The Chairman observed that the measures were informed by the Committee's concern on outlook and uncertainty in the political environment, which was fuelling insecurity. He reiterated the need to make the point clear that the economy was affected not only by monetary and fiscal policies but by other uncertainties so that those issues should be addressed as well. The action was seen as a normalisation process so that by March, 2011, the MPC would be able to gauge the outcome of its actions.

Summary of Decisions of the Meeting

After deliberations, the Committee voted to:

i) raise MPR by 25 basis points from 6.25 per cent to 6.50 per cent with immediate effect;

ii) maintain the symmetric corridor of +/-200 basis points, implying a Standing Lending Facility (SLF) rate of 8.50 per cent and Standing Deposit Facility (SDF) rate of 4.50 per cent.

iii) raise the Cash Reserve Requirement (CRR) Ratio by 100 basis points from 1.00 per cent to 2.00 per cent with effect from February 1, 2011; and

iv) raise the Liquidity Ratio (LR) by 500 basis points from 25.00 per cent to 30.00 per cent with effect from March 1, 2011.

v) It was also agreed that subsequent meetings would devote some time, where relevant, to review the effects of the policies implemented.

Any Other Business

9) The Chairman in an apparent effort to answer the question posed by Danladi Kifasi on why banks were not usually disposed to lending to the real sector, held some discussions with MPC members on current efforts being made to de-risk the industry and get banks to lend to the real economy. This was because, a bank would only lend if it was satisfied with the risk criteria. Consequently, the CBN was pursuing other routes that would help to address bottlenecks including legal issues. To that effect, he cited the alternative dispute resolution bill that was trying to address that problem. He also informed members that seven value chains in agriculture, namely, rice, maize, cotton, tomatoes, cassava, cattle and soya beans have been identified. Moreover, a steering committee which has the Ministers of Finance, Agriculture and Commerce as members was being set up and is to be chaired by him. The committee would attempt to find ways of unlocking credit to the real sector. But these are issues that go beyond monetary policy and require concerted efforts for effective results. That was why the Chairman viewed the recent

lifting of ban on tooth picks and furniture as a breach of contract and portends lack of credibility on the side of government. He remarked that the CBN saw no urgency in that policy and wondered why the policy should be reversed without warning. He regretted that as a result of that action, banks now establish LCs for the importation of furniture from abroad.

Reacting to the Chairman's observations, Danladi Kifasi remarked that those decisions were based on discussions with relevant stakeholders. He also said that one of the reasons for lifting the protection was to replace it with a levy, as it was discovered that some importers prefer to import through other ports leading to loss of revenue by government. The Chairman remarked that some of the consultations took place after the pronouncements.

In conclusion, the Chairman observed that for effectiveness, monetary and fiscal authorities have to work together. He stated that the quantitative easing and low interest rate policies were pursued to assist government when there was no risk to inflation. However, since there was inflationary risk, the CBN could not do otherwise, unless there were compelling reasons to do so. Consequently, the government could either reduce expenditure or find ways to increase its revenue but not to take recourse to printing of more money.

Date of Next Meeting

10.) The next meeting was scheduled to hold during March 21- 22, 2011.

Closing

11.) The meeting ended at 11.45 a.m. with a prayer by the Chairman, Sanusi Lamido Sanusi, Governor, Central Bank of Nigeria.

………………………….. ……..…………………………..

CHAIRMAN

SECRETARY

…………………………………….

DATE