PRESS RELEASE

CENTRAL BANK OF NIGERIA COMMUNIQUE NO. 50 OF THE MONETARY POLICY COMMITTEE, JUNE 5, 2007

The Monetary Policy Committee of the CBN met on 5th June 2007 and decided to reduce the MPR by 200 basis points, i.e., from 10.0 per cent to 8.0 per cent

1) The Monetary Policy Committee (MPC) met on 5th June, 2007 and reviewed the major macroeconomic developments and the implementation of fiscal, monetary and exchange rate policies in the first five months of 2007, as well as the challenges for the rest of the year. The meeting, the second in 2007, lasted three hours. The MPC noted with satisfaction the macroeconomic performances in the first five (5) months, as inflation and naira/dollar exchange rates stabilized further. It however, noted the potential threat to inflation. The Committee, therefore, expressed its commitment to sustaining macroeconomic stability.

Key Macroeconomic Developments

2) **Inflation:** The MPC noted that the inflation rate stayed within single digit in the first four months of 2007. In particular, the year-on-year (headline) inflation dropped steadily from 8.5 per cent at end-December 2006 to 4.2 per cent in April 2007. The Committee also observed that although the current

estimates show that inflation would remain single-digit at the end of the second-quarter, inflation pressures still persist.

3) **Exchange Rate:** The MPC noted with satisfaction the continued stability of the naira exchange rate in the first five months of 2007 as the naira remained stable at both the wDAS and the BDCs during the period. The naira exchange rate in the wDAS moved between ₦126.60/US$1 and ₦128.29/US$1 (rate +1%) in January through May, 2007. In addition, the premium between the wDAS and BDC rates narrowed from 1.39 per cent in January to 1.2 per cent in May 2007. The Committee noted the positive impact of the stability in exchange rate on the economy generally, particularly in locking-in inflationary expectations. Thus, the MPC reaffirmed its commitment to sustain the liberalization of the foreign exchange market.

4) **External Reserves:** From $41.96 billion at end December 2006, gross official reserves rose to $43.48 billion as at 28th May, 2007, which could finance 25 months of imports. The Committee, however, noted the risk to growth of reserves arising from the decline in the volume of crude oil production due to disturbances in the Niger Delta, but welcomed the initiatives of the government to resolve the crisis.

5) **Growth in Monetary Aggregates:** At the end of the first quarter, 2007, broad money grew by 8.80 per cent and moderated to 7.70 per cent at end-

April 2007, which when annualized showed a growth of 23.0 per cent compared with the target of 19.0 per cent for entire 2007. The rise in M2 was attributable to the combined effects of the increases in foreign asset (net) of the banking system and credit to the private sector.

6) **Credit**: Growth in aggregate domestic credit (net) declined by about 63.7 per cent at end-March, and by 38.7 per cent in April, 2007 relative to its level at end-December 2006. The fall in aggregate credit was attributed mainly to the decline in credit (net) to government during the period. Meanwhile, credit to the private sector grew by about 24.0 per cent in first four months ending April 2007, reflecting a growth of 72.0 per cent on annualized basis. The target for the year is 30.0 per cent. The Committee noted, however, that a significant proportion of the credit went into import financing, which have low inflation risk for the domestic economy. The spending items included payments for Telecommunications and Information Technology imports and the payment for oil blocs in foreign currencies.

7) **Reserve Money:** At end-March, the reserve money (N841.0 billion) was on target under the PSI programme. In April 2007, however, reserve money rose to ₦896.0 billion, while the forecast to end-June 2007 is about N926.50 billion, which is higher than the PSI target by N66.5 billion. The surge in reserve money is attributable to the expansion in demand for currency and

growth in banks' balances with the CBN. The MPC, therefore, stressed the need to intensify liquidity mop up operations to reduce the excess liquidity. It also agreed to apply some price and non-price disincentives to encourage banks to be more professional in their liquidity management.

8) Interest Rates Developments: The introduction of the CBN Standing Facility since December 2006 has continued to moderate the volatility in inter-bank rates in the first five months of 2007. In particular, the average inter-bank call rate moderated from 8.98 per cent in December 2006 to 7.54 per cent in April and to 7.6 per cent in May 2007. The decline in rates was due to the continued surfeit of funds in the market. With the year-on-year inflation rate at 4.20 per cent in April 2007, the inter-bank rates and other rates in the banking system have become strongly positive

OUTLOOK FOR REST OF 2007 AND MPC DECISIONS

The MPC noted that though inflation has moderated significantly, the downside risk remained. The Committee also noted the challenges in achieving the exit target reserve money by end-June, 2007; the rising autonomous private inflows and the risk of over-appreciation of the naira/dollar exchange rate.

The Committee, however, noted that the upside risk was strong. These included the continued stability of the exchange rate; the strong external sector reserves as well as the recent maiden broadcast of Mr. President to the Nation on sustaining the economic reforms. On the whole the Committee believes that the medium term outlook is one of robust economic performance.

Against this background the Committee decided to:

a) Introduce tenured repo at MPR

b) Reduce the MPR by 200 basis points, i.e. from 10.0 per cent to 8.0 per cent

c) Reduce the width of the interest rate corridor from +/- 300 to +/- 250 basis points.

    The combined implication of (b) and (c) is that the deposit facility now stands at 5.5 per cent while the lending facility would be 10.5 per cent, both down from 7 and 13 per cent, respectively.

d) Both facilities are expected to be used as a last resort. Consequently the frequent usage of these facilities will attract penalty.

e) Increase the issuance of primary market instruments to mop up about N100 billion;

f) That inter-bank placements shall henceforth form part of the deposits for calculating banks' liquidity ratio and

g) Continued use of open market operations (OMO) in liquidity management

Thank you for your kind attention.

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