

CENTRAL BANK OF NIGERIA COMMUNIQUE NO. 53 OF THE MONETARY POLICY COMMITTEE, DECEMBER 4, 2007

The Monetary Policy Committee of the CBN met on 4th December 2007 and decided to raise the MPR by 50 basis points from 9.0 percent to 9.5 per cent.

- 1) The Monetary Policy Committee (MPC) met on 4th December, 2007. The Committee reviewed the major macroeconomic developments and the implementation of fiscal, monetary and exchange rate policies in 2007, as well as the challenges for the first quarter of 2008. The MPC noted both the global and domestic economic and financial developments and how they influenced macroeconomic environment in 2007. The Committee noted with satisfaction the sustained single –digit inflation throughout the year and the orderly functioning of the foreign exchange and domestic financial markets.
- 2) It however, acknowledged the pressure of appreciation on the naira exchange rate which arose principally from the sustained high foreign exchange inflows buoyed by the favorable macroeconomic environment, investment climate as well as high rates of return in domestic financial markets. The Committee restated its commitment to ensuring continued price and monetary stability through an appropriate monetary policy stance for the rest of the year.

Key Macroeconomic Developments

- 3) **Inflation:** The Committee noted with satisfaction the decline in year-on-year (headline) inflation from 6.4 per cent in June 2007 to 4.1 per cent in September, 2007. In October, however, the year- on- year inflation rose slightly to 4.6 percent reflecting increases in the prices of utilities, transport, hotel and tourism and education. Staff projections indicate that the year –on- year headline inflation would move to 6.8 percent in November and further

- up to 7.3 per cent by year-end due mainly to year-end demand pressures. This is expected to moderate in the first quarter of 2008.
- 4) **Exchange Rate:** The MPC noted the steady appreciation in the Naira exchange rate, particularly in the second half of 2007. The effective Naira exchange rate at the wDAS appreciated from N127.43/US\$1 in June to N124.28/US\$1 in September and further to N120.63 /US\$1 in November 2007. Relative to the end-December 2006, the Naira has thus far appreciated by about 7.0 per cent. The Committee noted the rising private foreign exchange inflows and the increased demand for the Naira as key factors which contributed to the Naira appreciation.
 - 5) **External Reserves:** The Committee observed that the gross official reserve has increased to about US\$50 billion in November, 2007. This represented an increase of 18.06 per cent when compared with the level of US\$42.42 billion in the corresponding period of 2006. The level of reserves, the Committee noted, could support approximately 23 months of current foreign exchange disbursements.
 - 6) **Monetary Aggregates:** Over the end- December, 2006 level, broad money (M2) grew by 21.3 and 25.31 percent in September and October, 2007. When annualized the M2 grew by 28.44 and 30.25 percent, respectively in the two months, compared with 33.3 and 39.6 percent, respectively in the corresponding months of 2006. The growth of M2 was driven by the increase in foreign assets(net) of the banking system as well as the rapid rise in credit to the private sector since the end of the second quarter . Going by recent, both M2 and reserve money may be within targets for the year.
 - 7) While the Committee expressed concern about the rapid growth of M2, it however, noted with relief that this did not translate to higher inflation during the year, partly on account of the sharp increase in non-oil output.

- 8) **Credit:** The Committee noted that credit to the private sector maintained an upward trend in most of 2007. Credit to the private sector as at end-October 2007 relative to the level at end-December 2006 grew by 72.2 per cent. Staff projections through end-December 2007 indicate that private sector credit would grow by 49.5 per cent over end-2006 level.
- 9) **Interest Rates:** The MPC observed that the volatility in the inter-bank short-term rates continued to ameliorate during the year, as rates fluctuated within the interest rate corridor up to October when it was reviewed. Although the average inter-bank rate trended slightly upwards thereafter, it has remained generally below the MPR.
- 10) **Fiscal Stance:** The Federal budget for 2008 has projected significant increases in expenditure on account of build-up of infrastructure, environmental protection and social safety nets. As these expenditures take time to yield results, there would in the interim period be an impact on aggregate demand. The private sector's own investments in partnership with those of the public sector would also have lagged effects on output.

FUTURE OUTLOOK:

The MPC noted that the overall macroeconomic picture in 2007 has reflected improved stability; just as the prospects for the first quarter 2008 appear good. The Bank's projections show that the year-on-year (headline) inflation could remain single-digit in the first quarter of 2008, provided CBN continues to take proactive steps to manage the liquidity surfeit. There remains a strong upside risk to inflation in the near-term due to expected large capital inflows and significant fiscal injections.

DECISIONS:

In anticipation of the imminent fiscal surge and continuing capital inflows; and in order to drive core inflation down to single-digit as well as to sustain headline inflation along its present path, the Committee decided to take the following proactive actions:

- a) Issue new primary instruments to mop up a significant portion of the anticipated excess liquidity in the system.
- b) Continue with the regular open market operations (OMO)

- c) Raise the MPR from 9.0 percent to 9.5 percent - to signal a tightening of monetary policy stance.

Thank you for your kind attention.

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