



**Central Bank of Nigeria Communique No. 99 of the Monetary Policy Committee Meeting of Monday 19th and Tuesday 20th January, 2015**

The Monetary Policy Committee (MPC) met on January 19 and 20, 2015 against the backdrop of challenging external conditions and downside risks in the domestic economic environment. In attendance were all the eleven members of the Committee. The Committee reviewed key external developments as well as domestic economic and financial conditions and outlook for 2015.

**International Economic Developments**

The Committee noted the tepid recovery of the global economy in 2014. The major impetus for global growth in 2014 came from the U.S, and supported later in the year by the drop in oil prices. However, both developments fell short of returning the global economy to the pre-crisis growth path. This was mainly due to the weakness in Europe and the much slower pace of expansion in the emerging market

economies in particular. Specifically, global growth continues to be constrained by a number of old and new adversities including high debt and rising unemployment in many countries (both industrialized and developing), geopolitical tensions and conflicts; the negative impact of commodity price shocks on commodity exporting countries; weak external demand; and the tapering and eventual exit of the US Federal Reserve Bank from quantitative easing; triggering sharp corrections in the financial markets. Consequently, global output rose by about 3.3 per cent in 2014, which was the same rate of growth attained in 2013. It is estimated to strengthen to about 3.5 per cent in 2015.

The Committee, however, noted many downside risks to the outlook. The Euro Area and Japan appear trapped in low inflation and low growth conditions. High unemployment and debt could persist much longer in the Euro Area in particular while a possible deflation is likely if inflation continues on the downward trend. The Committee also acknowledged the high likelihood of an increase in interest rates in

the United States; which portends negative consequences for emerging and frontiers economies. Already, growth is moderating in most industrial countries and could further be dampened by the strengthening of the U.S dollar, more volatile capital flows and financial system vulnerabilities arising from currency depreciations. All of these could be compounded by increased geopolitical risks arising from the Ukrainian stand-off, militant terrorism, armed insurgency and the aftermath of the Ebola epidemic in some countries in the West African sub-region. Furthermore, the divergence between the US and Euro Area monetary policy stance, non-inclusive growth and the regional impact of falling oil prices with acute revenue shortages in countries like Nigeria, Venezuela and Russia add to the risk factors.

Evidently, the outlook for growth in the various economic clusters continue to be shaped by the identified risks and opportunities. The IMF projects the major advanced economies to grow at a modest pace of about 2.3 per cent in 2015, premised on the sustained growth in the U.S and some improvements in Europe. The decision of

the European Central Bank (ECB) to continue with the existing provision of unlimited short-term liquidity as well as the implementation of new programmes will be critical to the global economic performance in 2015. For the emerging markets and developing economies, growth could be modestly maintained in 2015 at about 4.3 per cent, driven essentially by domestic consumption and increased investment as net exports continue to moderate in response to softening commodity prices.

Inflation is not an immediate global priority as most of Europe and Japan grapples instead with potential deflation and high unemployment. The outlook for monetary policy suggests continued divergence amongst the various economic blocs. The Euro Area and Japan are expected to sustain this accommodative monetary policy stance while the U.S authorities appear to be leaning towards monetary tightening. Similarly, monetary policy is likely to remain restrictive amongst developing and emerging economies in order to stabilize the local currency, and to rein-in potential inflation

pressures. The Committee was generally of the view that monetary policy play a pivotal role in restoring economic activity to optimum levels globally, especially when complemented by structural reforms, fiscal adjustments and better coordination of policy actions. In fact, current conditions call for engagement of multiple macroeconomic and structural policy levers.

## **Domestic Economic and Financial Developments**

### **Output**

The National Bureau of Statistics (NBS) estimated real Gross Domestic Product (GDP) growth rate at 6.23 per cent in the third quarter of 2014 compared with 6.54 per cent in the second quarter. The Committee noted the continued dominance of the non-oil sector, particularly Services which contributed 2.53 percentage points, Agriculture (1.21 per cent) and Trade (1.08 percentage point). The Committee noted with satisfaction the Federal Government's efforts to boost power generation and supply, among others, which would

improve the economy's job creation prospects in the medium- to long-term.

The Committee was, however, concerned about the weakening contribution of the oil sector to overall growth, which is now being exacerbated by the rapid drop in oil prices since June 2014. In addition, the Committee noted that the security challenges in some parts of the country might also be contributing to the dampening effects on overall growth in the country.

## **Prices**

Headline inflation at end-December 2014 was 8.0 per cent, which was within the range of 6.0-9.0 per cent benchmark for inflation set by the Bank. The inflation recorded in December 2014 reflects a reduction in core inflation, seasonal factors related to the Yuletide celebrations, as well as the stabilization in food prices. The Committee, however, recognized some upside risks to inflation in the near-term including the likely higher import prices on the strength of an appreciating dollar and possible food supply bottlenecks linked

to insurgency and insecurity in some major agricultural zones of the country.

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

Broad money supply (M2) grew by 7.29 per cent at end-December 2014 over the level in 2013. This represented a marked improvement over the 1.32 per cent increase in 2013, but lower than the benchmark of 15.02 per cent for 2014. The relatively slower growth of total monetary liabilities (M2) reflected developments in both credit to government and the net foreign assets (NFA). During the period, credit to government contracted by 21.8 per cent, far below the growth benchmark of 28.4 per cent. Similarly, the NFA declined by 15.02 per cent. Credit to the private sector, however, grew by about 12.1 per cent, essentially pushing aggregate domestic credit growth of about 11.0 per cent. The weak performance of NFA was largely due to the lower oil prices with the attendant consequence of reduced accretion to external reserves. The Committee welcomed the posture of fiscal policy, which reflected in the decline in credit to

government coming especially at a time when government revenue was greatly pressured by adverse oil price developments. The Committee noted that this orientation of fiscal policy would have an overall beneficial effect by leaving DMBs with greater room to support the real sector with the much-needed credit. The Committee encouraged the Management of the Bank to continue to implement measures aimed at providing support to enable increased flow of credit to the private sector.

Interest rates in all segments of the money market trended upward between 26<sup>th</sup> November 2014 and 13<sup>th</sup> January 2015. The interbank call rate opened at 8.98 per cent on 26<sup>th</sup> November 2014 and closed at 26.15 per cent on 16<sup>th</sup> January 2015. Similarly, the OBB and 30-day NIBOR increased from 10.2 and 11.38 to 23.46 and 11.63 per cent, respectively during the period. The significant increase in these rates particularly for interbank and OBB was mainly due to the further tightening measures introduced at the November 2014 meeting of the MPC.

The Committee observed that the bearish conditions in the capital market continued as the equities market indicators trended downwards in the review period. The All-Share Index (ASI) declined by 16.1 per cent from 41,329.19 to 34,657.15 between December 31, 2013 and end-December 2014. Similarly, Market Capitalization (MC) decreased by 13.2 per cent from ₦13.23 trillion to ₦11.48 trillion during the same period. The Committee noted that the downward trend has continued into January 2015 as, year-to-date, both have declined by 16.2 and 15.7 per cent, respectively. Although this phenomenon is driven by global economic conditions, in Nigeria in particular, the situation is exacerbated by declining oil prices as foreign portfolio investors divest from the country. These developments call for closer monitoring and proactive interventions by all institutions concerned. The Committee reiterated its commitment to sustaining and deepening measures aimed at fostering confidence and stability in the financial system.

## **External Sector Developments**

The Committee noted that significant pressure persisted in the foreign exchange market during 2014 resulting in further weakening of the Naira across the three segments of the markets. The exchange rate at the rDAS-Spot opened at N157.34/US\$ (including 1% commission) and closed at N164.08/US\$, representing a depreciation of N12.34 or 4.28 per cent. The inter-bank selling rate opened at N165.7/US\$ and closed at N180/US\$, representing a depreciation of N14.73 or 8.63 per cent in the period, while at the BDC segment, the selling rate opened at N170/US\$ and closed at N191.50/US\$ representing a depreciation of N21.50k or 12.64 per cent.

Gross official external reserves as at December 31, 2014 stood at \$34.25 billion compared with \$42.85 billion at the corresponding period of 2013. The decrease in the reserves level was driven largely by increased funding of the foreign exchange market interventions to stabilize the exchange rate in the face of decline in reserve

accretion. The country's external reserves as at end-December, 2014 could finance 7.44 months of imports.

## **Considerations**

The Committee noted with satisfaction the growth performance of the economy as well as the year-end inflation outcome. It was, however, concerned about a number of risks including the security challenge in parts of the country, which has continued to disrupt farming and related activities; and the sustained decline in oil GDP. With regard to inflation, the Committee noted the recurring challenge of excess liquidity in the banking system and the possible complications arising from capital flow reversal, as well as the demand pressure in the foreign exchange market.

On the external front, falling oil prices, slowing global output recovery, divergent monetary policy postures between the US and Euro Area as well as non-inclusive growth remain very important risks.

The gradual normalization of monetary policy by the US Federal Reserve could exacerbate the current retrenchment of portfolio flows and increase pressure on currencies in emerging and developing countries including Nigeria.

In the light of the above considerations, the Committee observed that its decisions of November 2014 needed time for the effects to crystallize in the economy and therefore, voted to retain the current position.

Consequently, the Committee decided as follows:

**Decision**

- (1) All eleven members voted to retain the MPR at 13 per cent; retain the CRR on Private Sector deposits at 20 per cent; retain CRR on Public Sector deposits at 75 per cent; and retain the liquidity ratio at 30 per cent.
- (2) One member, however, voted for an asymmetric corridor around the MPR.

I thank you all for Listening

**Godwin I. Emefiele, CON**

Governor

Central Bank of Nigeria

**20<sup>th</sup> January, 2015**