A Rare Opportunity to Restore Confidence:

We think the MPC meeting of May 23-24, 2016 offers a rare opportunity for the MPC to stimulate the economy through appropriate monetary policy.

We expect the Monetary Policy Committee (MPC) to adjust the exchange rate to a level that reflects the current economic fundamentals of Nigeria. We also expect an adjustment in the Monetary Policy Rate (MPR) to a level that will produce positive real yields in the financial market. These two measures are important to stimulate investors' confidence in the Nigerian economy and financial market. **We think the MPC meeting of May 23-24, 2016 offers a rare opportunity for the MPC to stimulate the economy through appropriate monetary policy. We project an exchange rate of US$1/N275 with a band of +/-5%; and an increase in the MPR to 14% with a band of +/-2%.** At the end of its March 2016 meeting, the MPC increased the Monetary Policy Rate (MPR) to 12% from 11% and maintained the asymmetric corridor at +200basis points and -700basis points; increased the Cash Reserve Requirement (CRR) to 22.50% from 20%. It retained the Liquidity Ratio at 30%.

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On a global level, the global economy is still faced with a weak recovery path. The Organization of the Petroleum Exporting Countries (OPEC) maintained its global growth forecast at 3.1% for 2016. It expects an improvement in the momentum of the global economy in Q2 2016, driven majorly by recovery in the U.S., after very low growth in Q1 2016. **The weak and fragile growth from China and India means that the demand for crude oil will remain weak.** This means that oil price may not maintain a strong growth in the short-term with adverse impact on the Nigerian economy.

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The economic growth in Nigeria remains slow and below historical performance. The Gross Domestic Product (GDP) was 2.79% in 2015, compared with 6.22% in 2014. There are expectations of a pick-up in economic activities for the remainder of 2016 because of clearer fiscal policy direction. However, there are new threats in the economy, particularly from the resurgence of pipeline vandalism in the Niger Delta region. **Therefore, a bold monetary policy announcement to reflect the economic realities will enable investors to take investment decisions that can stimulate economic growth.**

A restrictive monetary policy stance is consistent with the current and short-term outlook of inflation rate.

The inflation rate has been trending up since January 2016. We expect the recent increase in fuel pump price to increase the inflation rate further from May 2016. The inflation rate in April 2016 increased to 13.72%, from 12.77% in March 2016. **A restrictive monetary policy stance is consistent with the current and short-term outlook of inflation rate.**

The prospect for acceleration in the rate of decline of U.S. crude production has partly buoyed crude oil prices in recent weeks. Other factors are the weaker U.S. Dollar, supply disruptions and forecasts for a sharp fall in non-OPEC production. Nevertheless, fundamentally, oversupply still persists, as oil output remains high. **The price of Bonny Light crude oil increased by 20.39% to US$49.54/b as at May 17, 2016 from US$41.15/b on March 22, 2016.** Nigeria's Crude oil production has fallen due to renewed pipeline vandalism. This has serious implication for the fiscal position of the government. **An adjustment in the exchange rate to US$1/N275 will give the government additional Naira revenue from oil exports.**

We expect a change in the exchange rate policy of the CBN to boost the external reserves through inflows from foreign investors.

The external reserves have not benefitted from the increase in oil price because of the strong demand for foreign exchange and the drop in crude oil production. The 30-day moving average external reserves declined by 4.38% from US$27.88bn at the last MPC meeting to US$26.66bn as at May 17, 2016**.** **We expect a change in the foreign exchange rate policy of the CBN to boost the external reserves through inflows from foreign investors.**

The value of the Naira remains weak because of the excess demand over supply.

The value of the Naira remains weak because of the excess demand over supply. Following the announcement of a new pump price, the value of the Naira depreciated further at the parallel market. The parallel market rate depreciated by 9.58% to US$1/N355 as at May 16, 2016 from US$/N321 before the announcement of the increase in fuel price. The CBN official market rate remains at US$1/N197. We believe the official exchange rate of US$1/N197 is almost redundant at the moment as few or no transaction is carried out at the official exchange rate. **An adjustment in the exchange rate is imperative to align the rate with economic realities.**

The spiralling inflation rate in three consecutive months has worsened the real yields on fixed income

The average yields on the 91-day, 182-day and 364-day Nigerian Government Treasury Bills (NTBs) increased to 7.12%, 9.25% and 10.95% in April 2016, compared with 5.73%, 8.27% and 10.17% respectively in March 2016. The yields on the 91-day, 182-day and 364-day NTBs stood at 8.27%, 9.64% and 14.25% respectively as at May 18, 2016. The yield on the 16.39% FGN Bond January 2022 also increased to 11.79% in April 2016 from 11.47% in March 2016, while it stood at 14.45% as at May 16, 2016. **The spiralling inflation rate in three consecutive months has worsened the real yields on fixed income securities.** We note that the yield on the 364-day NTB is higher than the inflation rate for the first time since November 2015. **We expect an increase in the MPR with the aim of reducing the inflationary pressure and to attract investments into the fixed income securities market.**

We expect an adjustment of the exchange rate to about US$/N275 and an increase in the MPR to 14%.

Looking at the macroeconomic developments in the economy, there are compelling reasons to believe that the MPC members will vote to increase the MPR to 14%, with symmetric corridor of +/-2%; adjust the exchange rate to US$1/N275, with a symmetric corridor of +/-5%; and equally re-open the inter-bank foreign exchange market.

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