Time for a Policy Change?

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We expect the Monetary Policy Committee (MPC) of the Central Bank of Nigeria (CBN) to hold rates at the current levels when the Committee meets on May 22 and 23, 2017. Although the current growth rates in monetary aggregates are below CBN's targets (which should justify an expansionary monetary policy), more stability in the foreign exchange market and lower inflation rate are necessary conditions for a policy change. At its March 2017 meeting, the MPC maintained the Monetary Policy Rate (MPR) at 14%, with the asymmetric corridor at +200 and -500 basis points; retained the Cash Reserve Requirement (CRR) and Liquidity Ratio (LR) at 22.50% and 30% respectively.

IMF forecasts global growth at 3.5% in 2017.

According to the International Monetary Fund (IMF), the global economy gained speed in Q4 2016 and the momentum is expected to persist in 2017. The IMF forecasts that global economic growth would increase from 3.1% in 2016 to 3.5% in 2017 and 3.6% in 2018, slightly above the October 2016 World Economic Outlook (WEO) forecasts. The major drivers are the buoyant financial markets and a long-awaited cyclical recovery in manufacturing and trade. **The positive outlook for the global economy should have a positive impact on the Nigerian economy through increased demand for its exports – particularly crude oil.**

The Fed maintained the Fed Rate at the range of 0.75% - 1.00%.

The Federal Open Market Committee (FOMC) of the United States (U.S) Federal Reserve (The Fed) maintained the Federal Funds Rate (The Fund Rate) at its May 2017 meeting. The Fed maintained the Fed Rate at a range of 0.75% - 1.00%. The unemployment rate in the U.S dropped to 4.4% in April 2017, below the 6.5% target while the inflation rate decreased to 2.2% in April 2017 but above the 2.0% target. Meanwhile, the U.S Gross Domestic Product (GDP) stood at 0.7% in Q1 2017, from 2.1% in Q4 2016. **There are high expectations of a further increase in the Fed Rate in the U.S in 2017. This may cause an increase in global yields with its adverse effects on Nigeria. Thus, the current restrictive policy is appropriate.**

The Nigerian economy is already showing signs of recovery in 2017. A review of the latest Purchasing Managers' Index (PMI) that the CBN published for the month of April 2017 suggests that the Nigerian economy is on the way out of recession. However, we believe more policies are required to achieve a sustainable growth. The PMI report shows that the Composite Manufacturing Index (CMI) expanded for the first time in the year 2017 and attained the highest level so far in the year 2017. The PMI report also shows that the production level in the manufacturing sector expanded for the second consecutive month, increasing to 58.5 points in April 2017 from 50.8 points in March 2017. PMI below 50 points level suggests a decline in business activity, PMI higher than 50 points level suggests an expansion while PMI at the 50 point level suggests no change. **We believe the increase in PMI is sustainable in the short to medium-term provided policies that increase access to credit and create an enabling business environment are pursued.**

The FGN decision on price of PMS and electricity tariff may impact inflation rate.

The inflation rate (Year on Year) dropped to 17.24% in April 2017, from 17.26% in March 2017. The fall in the inflation rate was mainly on account of base effect of previous year's increase in the Consumer Price Index (CPI) and the stabilising effect of foreign exchange rate. The stabilising effects of the current high food and non-food product prices also led to a decrease in the inflation rate in April 2017. **Although we expect the inflation rate to trend downward for the rest of 2017; the level of drop will depend on Federal Government of Nigeria (FGN) decision on fuel price and electricity tariff. The inflation rate at 14.24% and our projection that it may remain high in the short-term may not justify a rate cut at the May 2017 meeting.**

There are strong indications that the OPEC and non-OPEC oil output cut would be extended, possibly till March 2018.

The production data from the Nigerian National Petroleum Corporation (NNPC) shows that Nigeria's average oil output decreased by 18.13% to 1.58mbd in December 2016, from 1.93mbd as at November 2016. The oil production was affected by the shutdown of Trans Niger Pipeline (TNP) and Nembe Creek Trunk Line due to pipeline leakages, shut down of Agbami Terminal for mini turn around maintenance and the existing force majeure at Forcados and Brass Terminals. The Minister of Petroleum reported that the latest oil production figure is about 2mbd. The average price of Bonny Light was US$52.75/b in April 2017, an increase of 1.05% from the average price of US$52.20/b recorded in March 2017. Meanwhile, the price of Bonny Light crude oil decreased by 1.40% to US$50.04/b as at May 12, 2017 from US$50.75/b on March 21, 2017. **There are strong indications that the OPEC and non-OPEC oil output cut would be extended, possibly till March 2018. This will have positive impact on oil revenue but may place pressure on the current Premium Motor Spirit (PMS) price and higher inflation rate. Thus, a rate cut is not desirable given these conditions.**

The yields on the NTBs sold on May 03, 2017 were at 14.08%, 18.89% and 23.16% on the 91-day, 182-day and 364-day NTBs, respectively.

The consistent accretion to the external reserves has enhanced the capacity of the CBN to maintain stability in the foreign exchange market. The 30-day moving average external reserves increased by 1.75% from US$30.35bn as at March 21, 2017 to US$30.88bn as at May 12, 2017. **A cut in the MPR would put a negative pressure on the external reserve. Thus, a hold decision is appropriate.**

The Naira appreciated at both the inter-bank and parallel markets of the foreign exchange market between the last MPC Meeting and May 16, 2017. It recorded an appreciation of 0.67% at the inter-bank market to close at N305.45/US$ on May 16, 2017 from N307.50/US$ on March 21, 2017. The parallel market rate also appreciated by 12.31% to N390/US$ on May 16, 2017 from N438/US$ on March 21, 2017. The premium between the inter-bank and parallel markets averaged about N90 after the last MPC meeting in March 2017, from an average of N180 during the period between the January and March 2017 meeting. **There are still a number of uncertainties surrounding the stability of the foreign exchange. These uncertainties do not support a rate cut.**

The average yields on the 91-day Nigerian Government Treasury Bill (NTB) decreased to 14.05% in April 2017, from 14.08% in March 2017. However, the 182-day and 364-day closed higher at 18.94% and 23.23% in April 2017, compared with 18.81% and 22.81% in March 2017. The yields on the NTBs sold on May 03, 2017 were at 14.08%, 18.89% and 23.16% on the 91-day, 182-day and 364-day NTBs, respectively. Meanwhile, the average yield on the 16% FGN Bond June 2019 and 16.39% FGN Bond January 2022 increased to 16.01% and 15.85% in April 2017 from 15.79% and 15.80% in March 2017. The 10% FGN Bond July 2030 decreased to 15.86% in April 2017, from 15.90% in March 2017. **The funding for foreign exchange intervention in the inter-bank market dried up liquidity and led to increase in yields on fixed income securities. A rate cut may send confusing signals to the market.**

The monetary aggregates in Nigeria as at March 2017 show that the annualised growth rate in the money supply is below the targets the CBN sets for the year 2017.

The monetary aggregates in Nigeria as at March 2017 show that the annualised growth rates in the money supply are below the targets the CBN stipulates for the year 2017. The broad money supply (M2) declined by 7.17% in Q1 2017, lower than the provisional growth benchmark rate of 10.29% for 2017. Net Domestic Credit (NDC) increased marginally by 1.17% in Q1 2017, representing an annualised growth rate of 4.70% but significantly lower than the growth rate target of 17.93% for 2017. The credit to government increased by 8.17% in Q1 2017, representing an annualised growth rate of 32.68%, marginally lower than the target growth rate of 33.12% for the year 2017. However, expansionary monetary policy will be required when there is stability in the foreign exchange market and the inflation rate is moderated.

Table 1: Monetary Aggregates – N'mn

Month	Narrow Money	Quasi Money	Broad Money	Ratio of MI to M2	Net Domestic Credits	Net Credits to Government	Net Credits to Private Sector	Ratio of Private Sector Credits to Domestic Credits
	M1	QM	M2		-	-	-	
Mar-16	9,040,818	11,429,618	20,470,436	44%	22,664,816	3,782,578	18,882,238	83%
Apr-16	9,136,068	11,591,841	20,727,909	44%	23,312,346	3,933,735	19,378,611	83%
May-16	9,391,866	11,330,042	20,721,908	45%	22,852,137	3,803,178	19,048,959	83%
Jun-16	9,125,933	12,559,032	21,684,965	42%	24,318,143	2,893,190	21,424,953	88%
Jul-16	9,230,931	12,951,257	22,182,188	42%	25,159,363	2,784,110	22,375,253	89%
Aug-16	9,125,897	12,521,428	21,647,325	42%	25,955,106	3,290,896	22,664,210	87%
Sept-16	9,949,385	12,184,093	22,133,478	45%	26,341,471	3,748,843	22,592,628	86%
Oct-16	10,023,617	12,251,896	22,275,513	45%	26,774,684	3,705,049	23,069,635	86%
Nov-16	10,429,541	11,953,374	22,382,915	47%	26,848,256	3,802,861	23,045,396	86%
Dec-16	11,404,906	12,320,226	23,725,132	48%	27,153,880	4,806,982	22,346,898	83%
Jan-17	11,267,712	12,113,228	23,380,940	48%	26,627,285	4,284,261	22,343,024	84%
Feb-17	10,212,647	12,153,000	22,365,648	46%	26,771,070	4,408,656	22,362,414	84%
Mar-17	9,955,242	12,069,736	22,024,978	45%	27,472,687	5,199,693	22,272,995	81%
Growth : Dec16-Mar 17	(12.71%)	(2.03%)	(7.17%)		1.17%	8.17%	(0.33%)	

Source: Central Bank of Nigeria

Looking at the economic developments in Nigeria and the impact of external developments on the Nigerian economy, we expect the MPC to hold rates at the current levels. A change in the monetary policy stance that results in lower rates may be counterproductive to address the current high inflation rate. An expansionary monetary policy stance at this time may not also support a stable foreign exchange rate. The Nigerian economy should follow a sustainable path to recovery, with appropriate fiscal policy implementation

For enquiries please contact us at our offices:

***Lagos Office**: 5th-8th floors UAC House, 1/5 Odunlami Street. Tel: 234-1-2702881-2, 234-1-2702887*

***Port Harcourt Office:** 2nd Floor, Skye Bank Building (Former Mainstreet Bank Building), 5 Trans Amadi Road, Port Harcourt. Tel: 234-802 408 1331*

***Abuja Office:** Leadway House (1st Floor), Plot 1061 Herbert Macaulay way, Central Business District, Abuja-Nigeria. Tel.: 234-9-2918821*

Website:** www.fsdhgroup.com **Email:** research@fsdhgroup.com. **Our Reports and Prices are also Available on Bloomberg {FSDH<GO>}