



**CENTRAL BANK OF NIGERIA COMMUNIQUÉ NO 116 OF THE MONETARY POLICY
COMMITTEE MEETING OF MONDAY 20th AND TUESDAY 21st NOVEMBER, 2017**

Background

The Monetary Policy Committee met on the 20th and 21st of November, 2017 against the backdrop of a relatively optimistic global economic outlook. The Committee reviewed key developments in the global and domestic economies during the first ten months of 2017 and assessed the risks to price and financial stability in the short- to-medium term as well as outlook for the first half of 2018.

Nine (9) members of the MPC were present at the meeting.

External Developments

Global output is projected to improve to 3.6 per cent in 2017 from 3.2 per cent in 2016. The revised growth forecast reflects the uptick in global economic activity, strengthened by the recovery in oil and other commodity prices and leading to improved aggregate demand. Growth in the advanced economies is projected to improve to 2.2 per cent in 2017 from 1.7 per cent in 2016. Similarly, emerging markets and developing economies are

forecast to grow at 4.6 per cent in 2017 up from 4.3 per cent in 2016. The MPC, however, noted some risks to the outlook for global growth to include: continued tension in the Korean Peninsula, complexities arising from the BREXIT negotiations and financial market uncertainties due to monetary policy normalization in the US.

The Committee noted that the pace of increase in inflation in the advanced economies, with the exception of the UK, is expected to be considerably slow towards the end of 2017. In the emerging market economies, inflationary pressures have abated as key economies exit recession and their currencies stabilize. Inflation is projected at 1.7 and 4.2 per cent in 2017 in the advanced and developing economies, respectively. The Committee observed that the outlook for global monetary policy remains largely accommodative, in support of economic recovery and growth.

Domestic Output Developments

Data from the National Bureau of Statistics (NBS) indicate that real Gross Domestic Product (GDP) grew by 1.40 per cent in the third quarter of 2017, up from 0.72 per cent, and contraction of 0.91 per cent in the second and first quarter of 2017, respectively. The major drivers of real GDP growth were agriculture (0.88%) and industry (1.83%). Some subsectors contracted, including: construction (0.01%), trade (0.29%) and services (1.02%). Overall, non-oil real GDP contracted by 0.76 per cent in Q3 2017, giving credence to

the argument that more work is required to consolidate the recovery process; by putting in place policies that will boost growth through the non-oil sector.

The Committee also noted the continuous positive outlook based on the Manufacturing Purchasing Managers Index (PMI), which stood at 55.0 index points in October 2017, indicating expansion in the manufacturing sector for the seventh consecutive month. Eleven of the sixteen sub-sectors reported growth in the review period. Also, the composite PMI for the non-manufacturing sector stood at 55.3 index points in October 2017, indicating growth for the sixth consecutive month. The Committee hopes that, while the economic recovery appears to remain fragile, a tenacious implementation of the 2017 budget and quick passage of the 2018 budget would boost aggregate demand and confidence in the economy.

Developments in Money and Prices

The Committee noted that money supply (M2) contracted by 5.54 per cent in October 2017 (annualised), in contrast to the provisional growth benchmark of 10.29 per cent for 2017. The development in M2 is largely due to the contraction of 37.50 per cent in other assets net (OAN). Similarly, M1 contracted by 7.79 per cent (annualised to -9.35 per cent). Net domestic credit (NDC) expanded by 1.18 per cent, annualized to 1.42 per cent, driven primarily by net credit to government, which also expanded by 7.60 per cent against the programmed growth of 33.12 per cent. Credit to the private

sector, however, contracted by 0.24 per cent in October 2017, compared with the provisional benchmark of 14.88 per cent. The MPC also noted the structural constraints in the transmission of credit to the real sector of the economy as well as the rising unemployment level. The Committee urged the Management of the Bank to continue to encourage the deposit money banks to accelerate the rate of credit growth to the real sector of the economy.

Inflationary pressures in the economy continued to moderate with headline inflation (year-on-year) receding for the ninth consecutive month to 15.91 per cent in October 2017 from 15.98 per cent in September 2017. Food inflation fell marginally to 20.31 per cent from 20.32 per cent in September, while core inflation increased slightly to 12.14 per cent from 12.12 per cent during the same period. These developments were attributable to the contraction in money supply, favourable but dwindling base effects, and the relatively stable naira exchange rate. In spite of the marginal decline in food inflation in October, the Committee noted that the rate remained high, traceable to cross border sales, distribution bottlenecks, high prices of farm inputs and supply shortages.

Money market interest rates oscillated in tandem with the level of liquidity in the banking system as the average inter-bank call rate, which opened at 12.00 per cent on October 3, 2017, closed at 5.38 per cent on November 16,

2017. The OBB rates opened at 10.41 per cent and closed lower at 6.02 per cent in the same period. However, the average inter-bank call and OBB rates for the period stood at 10.94 and 10.15 per cent, respectively. The development in net liquidity positions and flows reflected the effects of Federation Account payments to states and local governments; remittances by the Nigerian Customs, Federal Inland Revenue Services; OMO sales; foreign exchange interventions and maturing CBN Bills.

The Committee noted the continuing improvement in the level of external reserves and the equities segment of the capital market. External reserves grew to US\$34.9 billion at the close of business on November 16, 2017. Similarly, the All-Share Index (ASI) rose by 3.38 per cent from 35,504.62 on August 31, 2017 to 36,703.58 on November 17, 2017. Market Capitalization (MC) improved by 4.35 per cent to N12.77 trillion from N12.24 trillion during the same period. Relative to end-December 2016, capital market indices rose by 36.57 and 38.10 per cent, respectively, indicating rising investor confidence, due to improvements in foreign exchange supply.

Total foreign exchange inflow through the central bank declined by 6.61 per cent in October 2017, compared with the previous month and attributable to the decline in crude oil and gas receipts as well as revenues from petroleum profit tax (PPT) and royalty payments. Total outflows, however, increased by

18.77 per cent during the same period, as a result of interbank sales, direct payments and JVC calls.

The Committee noted the gradual convergence between the rates at the bureau-de-change (BDC) and the Nigeria Autonomous Foreign Exchange (NAFEX) market segments, as well as the stability of the exchange rate at the inter-bank segments of the foreign exchange market during the review period. Similarly, the Committee viewed with satisfaction, the growing patronage at the Investors' and Exporters' (I&E) window of the foreign exchange market and attributed the development to increased confidence by foreign investors and the preference of Nigerian investors' and exporters' for the window compared with all other windows. The MPC noted that the I&E window had increased liquidity and boosted confidence in the market with over US\$18.70 billion in transactions since its introduction in April 2017.

2.0. Overall Outlook and Risks

Forecasts of key macroeconomic variables indicate a positive outlook for the economy up to Q1 2018. This is predicated on continued implementation of the 2017 budget into early 2018, anticipated improvements in government revenue from the implementation of the Voluntary Asset and Income Declaration Scheme (VAIDS) as well as favourable crude oil prices. The development finance initiatives by the CBN in the real sector, particularly in agriculture, are expected to continue to yield positive results in terms of

output expansion and job creation. Focusing on the downside risks to the outlook, the Committee noted the low fiscal buffers and weak aggregate domestic demand. On the external front, widening global imbalances, and rising geo-political tensions were some of the crucial risks identified.

3.0. The Considerations of the Committee

The Committee noted with satisfaction the second consecutive quarterly growth in real GDP following five quarters of contraction. In addition, Members welcomed the relative stability in the exchange rate, particularly the narrowing premia and the very slow deceleration in consumer price inflation, largely attributable to base effects. Overall, the economy has begun to show strong signs of recovery as public investment has picked up with increased housing construction at the Federal and state levels, as well as shipping activities at the ports. The Committee was, however, of the view that policy makers must not relent in their aggressive policy initiatives aimed at continuing the positive growth trajectory. The Committee was also concerned about potential adverse external developments and the cautious approach to lending and financial intermediation by domestic deposit money banks.

The Committee similarly evaluated other concerns in the domestic economy and the opportunities for strengthening output recovery, noting that some highly critical subsectors were yet to resume growth. The Committee noted

the significant contribution of food prices to headline inflation and observed that the benefit of base effect on overall headline inflation had substantially dwindled. Members, however, expressed confidence that the tight stance of monetary policy and the stability in the exchange rate of the naira should continue to positively weigh in on price developments. The Committee reaffirmed its commitment to maintaining price stability, which is crucial to sustainable economic growth and development.

The Committee welcomed the review of the Economic Recovery and Growth Plan (ERGP), in an effort to realise the objectives of the plan. In the same vein, the Committee urges a quick passage of the 2018 Appropriation Bill by the National Assembly, so as to keep fiscal policy on track and deliver the urgently needed reliefs in terms of employment and growth of the economy.

On financial stability, the Committee noted the concentration of non-performing loans in a few sectors but observed that the overall condition and outlook for the banking system was stable as deposit money banks' balance sheets remained strong. This assessment is strengthened by developments in the national accounts and the expectations that the affected sectors are returning to growth. Nonetheless, the Committee urged further strengthening of supervisory oversight and deployment of early warning systems in order to promptly identify vulnerabilities and proactively manage emerging risks in the

banking system. The Committee further observed that government was increasing debt, both domestically and externally, thus crowding out the private sector.

4.0. The Committee's Decisions

In arriving at its decision, the Committee appraised potential policy options in terms of the balance of risks. The Committee also took note of the gains made so far as a result of its earlier decisions; including the stability in the foreign exchange market and the moderate reduction in inflation and thus extensively deliberated the options regarding whether to hold , tighten or ease the policy stance.

While tightening would strengthen the impact of monetary policy on inflation with complementary effects on capital inflows and exchange rate stability, it nevertheless could also potentially dampen the positive outlook for growth and financial stability. On the other hand, whereas loosening would strengthen the outlook for growth by stimulating domestic aggregate demand through reduced cost of borrowing, it could aggravate upward trend in consumer prices and generate exchange rate pressures. The Committee also feels that loosening would worsen the current account balance through increased importation. On the argument to hold, the Committee believes that key variables have continued to evolve in line with the current stance of macroeconomic policy and should be allowed to fully

manifest. Members noted that the developments in output and inflation in particular required effective close monitoring in order to gain clarity on the medium term optimal path of monetary policy.

In consideration of the foregoing, the Committee decided by a vote of 8 to 1 to retain the Monetary Policy Rate (MPR) at 14.0 per cent alongside all other policy parameters. One member voted to reduce the MPR by 100 basis points.

Consequently, the MPC voted to:

- (i) Retain the MPR at 14.0 per cent;
- (ii) Retain the CRR at 22.5 per cent;
- (iii) Retain the Liquidity Ratio at 30.0 per cent; and
- (iv) Retain the Asymmetric corridor at +200 and -500 basis points around the MPR.

Thank you for listening.

Godwin I. Emefiele

Governor, Central Bank of Nigeria

21st November, 2017

PERSONAL STATEMENTS BY THE MONETARY POLICY COMMITTEE MEMBERS

1. ADELABU, ADEBAYO

It is laudable that the economy has formally exited recession, justifying the various bold initiatives put in place by macroeconomic policy makers in the last couple of months. In tandem with this, headline inflation eased to 15.91 per cent in October 2017, sustaining the decelerating trend of the past nine months. In the external sector, the exchange rate has not only stabilized in both markets, but a good degree of net accretion to external reserves has equally been observed, taking the gross external reserves to about US\$34 billion in November, 2017 the highest level in the last two years. In this regard, it is worth commending the Investors' and Exporters' FX Window put in place by the Bank in boosting liquidity in the market. The innovation, among others, has substantially scaled up the bar of confidence of economic agents in the economy with the attendant self-reinforcing phenomenon.

The progress recorded so far, obviously, is impressive, but vulnerability is still visible, thus the issues now border on sustaining the trend, which essentially involves building resilience, while simultaneously reducing vulnerability. This, of course, is the area that poses considerable challenges to monetary authority and the entire macroeconomic policymakers. The risk factors to maintaining the trend are quite huge, cutting across the real, fiscal and, external sectors.

In the real sector, beside the fact that the current recovery is weak and naturally vulnerable to setback, other issues like rising spate of industrial unrest

and militancy activities are serious risk factors that could undermine growth prospects. In this regard, it is commendable that the Federal Government has set up a Presidential Committee on employment, which would proffer measures to harness the bundles of untapped human resource endowment and therefore assist the growth process. Without prejudice to this initiative, it needs to be borne in mind that an enduring growth process is equally dependent on the capacity to preserve existing level of growth in output. Against this perspective, it is expedient that appropriate framework be put in place to identify and monitor signals of labour unrest with a view to promptly addressing such before an escalation in order to prevent reversal of the ongoing recovery effort.

Another issue of serious concern within the real sector is the inflation dynamics. Although overall inflation is easing, it is quite disturbing that farm produce component is rising, reflecting supply bottlenecks particularly disruption to farming activities on account of several factors like flooding, militants in the North East, and displacement of many farming communities by herdsmen. One glaring issue from the analysis of risk factors within the real sector is that the issues are not much of monetary factors, but largely requiring structural policies and robust engagement with critical stakeholders. As such, the response of the monetary authority should essentially be maintenance of status quo ante.

The fiscal sector is equally fraught with a number of issues that could undermine macroeconomic conditions within the short to medium term. In

the first instance, although a causal examination of fiscal operations for the first half of the year shows an improvement, which is good for monetary policy, a deeper examination reveals a lot of outstanding obligations particularly to contractors. Settlement of these obligations could result possibly in further fiscal strain, extending the deficit beyond projection with the likely implication of additional borrowing and the attendant crowding out of the private sector credit.

On another but related dimension, the 2018 Appropriation Bill has just been presented to the National Assembly by the President. It is commendable that the Federal Government is keeping faith with the tenets of the Medium Term Expenditure Framework (MTEF) as witnessed in the increase in allocation to capital projects, while simultaneously making provision for sinking fund that would assist in redeeming maturing bonds. This approach would definitely mitigate key risks in macroeconomic condition particularly volatility in the financial markets. This notwithstanding, a budget of N8.6 trillion, predicated on deficit financing of about N1.7 trillion or about 20 per cent may likely trigger some other challenges to macroeconomic conditions. For one, public debt to GDP has been increasing consistently since 2012 and is now at 15.5 percent. The new borrowings would invariably increase the level of public debt, raising concern about sustainability. Furthermore, the structure of the new borrowings is a matter of concern. The deficit financing of N1.69 trillion is expected to be sourced equally between domestic and external markets. Each of these sources would exert significant pressure on domestic

macroeconomic conditions. From the external markets, although rising appetite for yield has strengthened the demand for debt instruments of emerging economies, the spate at which many sub-Saharan countries are slipping into debt distressed conditions has triggered a downgrade of their credit ratings below investment grade. The implication is that the new external borrowing in the budget would much likely attract higher interest rate thereby increasing the burden of debt servicing. The risks of borrowing from the domestic are fairly obvious. It is well-known that credit to the private sector has shown lackluster performance since the beginning of the year. For example, statistics revealed that credit to the private sector contracted by 0.24 per cent at end-October, annualizing to 0.288 per cent against the target of 14.88 per cent. This, of course is highly worrisome for an economy that is in economic recovery phase. The reason commonly adduced for this development is crowding out by the government sector. Beside the risk of crowding out, credit to private sector could suffer additional set back on account of asymmetry of information feature of Nigeria's credit market. This requires that the banking sector places considerable premium on collateral as reflected mostly by net worth of business firms and enterprises. Given that increase in government borrowing would increase the price of fixed income securities at the expense of equity, net worth of business firms and enterprises would nose-dive, prompting banks to scale down credit to the private sector. This, invariably would constitute considerable drag to the recovery process. In a nutshell, the evolving scenarios demand some sorts of fiscal consolidation

albeit without disrupting spending on public investments that are critical to addressing bottlenecks to growth process. In other words, efforts should be geared at raising revenues particularly from non-commodity sources while simultaneously cut down on recurrent expenditures.

In tandem with developments within the domestic economy, key indicators from the external sector have shown impressive performance in the last couple of months, but the buildup in the downside risks still remains very strong. Crude oil prices in particular have witnessed an appreciable increase due to waning excess supply and slowdown in US shale oil production as well as temporary shutdown of major refineries in the aftermath of the hurricane Harvey storm. This development has been reinforced by improved compliance of OPEC members with production cut deal. Although the deadline on the deal has been extended to the end of the first quarter of 2018, little is known about the next policy move to ensure that output does not exceed demand. The central issue here is that the current rally in the prices of crude oil is mainly driven by temporary factors and as such subject to setback.

On a related note, global inflation is beginning to show a divergence from the trend of the last three years. Global price level, which was largely subdued over the past three years due to weakness in energy prices, has commenced a fair degree of uptick. The latest projection by IMF revealed that global inflation would accelerate to 3.5 per cent in 2017 from 3.1 per cent in 2016, fuelled by the upsurge in oil prices and currency depreciation.

This suggests that domestic price dynamics is still confronted with the upside risk of international spillover even if the domestic monetary authority succeeds in containing exchange rate depreciation. Given the possibility of crystallization of this risk, the option of monetary easing should be treated cautiously at this moment.

Against the perspective of the foregoing analysis, the option of monetary easing at this period appears sub optimal, while further tightening may strain the macroeconomic environment, most especially in light of dismal performance of credit to the private sector. In view of the foregoing issues, I would like to vote for the retention of all the current monetary policy measures.

2. BALAMI, DAHIRU HASSAN

The picture at the global level shows that output growth momentum remained resilient due to recovery in commodity prices and aggregate demand, consequently IMF projected upward growth rate of 3.6 %. The main drivers of growth is coming from Euro area, Japan and Canada. In the emerging economies, growth is expected to come from China, Brazil and Russia. Likewise, in the LDCs countries such as South Africa, Kenya and Nigeria is where growth is expected to come in 2018. However, in Nigeria the year 2017 started on a bad footing with the economy still in recession; inflation at about 18.7%; unemployment of more than 14%; exchange rate of N525/to a dollar; a negative growth rate of -1.58%; and high prime lending rate of 30%. Taking the assessment of the growth performance by the MPC towards the growth of the economy, inflation has decelerated from 18.97% in January to 15.97% by September 2017. Exchange rate at both the interbank and the BDC has stabilised at about N305/366 to a dollar and currently there is south ward convergence. The economy was able to move out of the recession in the second quarter with a positive growth rate of 0.55%, followed by an improvement in the third quarter with 1.40% growth rate. However, this growth rate is not what MPC expected because Nigeria's population growth rate is about 2.82% implying that for growth to be meaningful it must be about 6%. The major factor driving growth in the economy out of the recession is the oil sector such as oil production and oil prices. However, both factors are fragile because volatility in the oil market is uncertain due to the following reasons:

US shale oil development and ability of the government to maintain stable peace in the Niger Delta region.

At the external sector, the flow of Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI) have improved and more than US\$ 10 billion have flowed in. However, managing the stability of the inflows is also a big constraint to growth because of the following factors: the normalisation of US economy and possibility of another hike in interest rate. Also, the increased protectionist policy or inward looking policies of most developed economies is a threat to Nigeria's growth. Although Nigeria has exited recession, the economy is currently experiencing in a stagflation, where unemployment is on the increase and high inflation in double digit. High inflation discourages growth. Again data and statistics show that the service sector of the economy, which has been a great contributor to GDP growth (50%) is still in recession. The other variables constraining growth in Nigeria include declining government revenues both in terms of foreign exchange receipts as well as domestically collected revenue through taxes; deteriorating infrastructural transportation facilities such as road, air, waterways and rail; problems of energy such as electricity, premium motor spirit (PMS), diesel; insecurity such as Boko Haram in the north east, and other terrorist activities particularly in Zamfara, Katsina, Benue and Niger Delta States etc. are all hindrances to growth.

To promote growth there is need to stimulate the economy. This can be achieved by employing appropriate monetary and fiscal policy tools to aid in the diversification of the economy through the following:

1. Demand management policies such as discouraging high levels of consumption of imported goods, which implies exporting jobs. It also reduces our level of reserves bringing in volatility in the foreign exchange market. The demand management policies earlier put in place such as the ban on the import of 41 commodities which can be produced in Nigeria from the interbank foreign exchange should be encouraged and maintained until the situation improves. This has helped reduce importation as well as saved foreign exchange which would have been expended on the importation of the banned commodities. This has also improved the Purchases Managers Index (PMI). The update from the FX market is encouraging in terms of FDI and FPI flow which was supported by MPCs tightening.
2. The developmental activities of the Bank should be encouraged with caution so that it does not come into conflict with one of the core mandates of the CBN that is maintaining price and foreign exchange rate stability and assisting Government in promoting the growth of the economy.
3. In the foreign exchange market a lot of interventions have been introduced in order to manage the available foreign resources. These include intervention, in the interbank foreign exchange segment,

Bureau de Changes (BDCs); and provision of windows for the Investors and Exporters; SMEs BTA/Medical Tourism; and school fees which greatly assisted in making foreign exchange available to clients thereby stabilising the foreign exchange market. The bank should also monitor carefully the activities of speculators, rent seekers, and round trippers, amidst escalated pressures so that they do not destabilise the market.

The impact of the policies put in place by the Monetary Policy Committee (MPC) has led to the drop in the level of imports into the economy and to the rising level of the external reserves.

Inflation has also moderated though not in the direction we wanted. It should be noted that food inflation is not coming down due to massive exportation of agricultural food items produced in the North to the neighbouring countries of Niger, Chad and Northern Cameroun. A lot of work need to be done until growth outweighs population growth. Typically, the CBN can target some big private sector investors to invest heavily in the agricultural sector.

The critical question to ask is "how do we reduce inflation and interest rate charged by the DMBs and how do we encourage banks to lend to the real sectors of the economy"? Interest rate should come down but at what point will it be appropriate to lower interest? What can also be done to reduce the high level of unemployment in the economy?

The overall assessment is that most of the variables such as inflation, growth of GDP, and stability in the foreign exchange market have attained some level of improvement. However, a lot need to be done. To my mind there is need to keep on with passive monetary policy so that the level of stability in the foreign exchange market, deceleration of inflation and rising growth which are all fragile must be guarded. I therefore do not support loosening at this time, because it will be inflationary and will disturb the relative stability in the foreign exchange market. At the same time tightening would not be admissible because it will hurt the economy. I therefore vote to hold, to wait for clarity to enable the fiscal side to do their job as well as to allow the past policies to work out as evident from the growth recorded in the second quarter of 2017 leading to the exit of the economy from recession. In view of this I recommend the following:

1. To retain the MPR at 14%
2. To retain the CAR at 22.5%
3. To retain the liquidity ratio at 30%
4. To retain the asymmetric corridor at +200 and -500 basis point around the MPR.

3. BARAU, SULEIMAN

Background

Relative to the take-off point at the beginning of the year, the Nigerian macroeconomic condition is assuming a better shape with a gradual correction of imbalances in various sectors. In particular, the hitherto sharp volatility in the foreign exchange market has been sufficiently contained, while the deceleration in inflation, which commenced in February, remained consistent. It is without gainsay that the evolving macroeconomic outcomes has benefited considerably from proactive macroeconomic policy measures as well as benign global economic condition, notably the latest rally in the price of crude oil.

More fundamentally, it is commendable that the Federal Government is keeping faith with the tenets of the medium term Economic Recovery and Growth Plan (ERGP) by taking some bold steps through the recent release of three Executive Orders (EOs). The EO on local content in particular would boost domestic economic activities and invariably tackle unemployment head-on. Equally commendable is the picture of the fiscal strategy as contained in the 2018 Appropriation Bill recently presented to the National Assembly by the President. Of significant importance is the increase in the allocation to capital projects to about 30 per cent, in line with the principles of ERGP. With full commitment to these measures, I am convinced that the ongoing recovery would remain on course.

From monetary policy perspective, the option of further tightening is practically out of the equation in view of the balance of risks in the medium term. This, in essence, reduces the options at this meeting to either easing or retaining the current monetary policy measures. I would prefer to vote for the retention of the current measures, based primarily on the need to strengthen the evolving stability in the macroeconomic environment and possibly address some risk factors, which have the potential to crystalize over the medium term.

Pressure Points

Global Environment

Recovery in the global economy is firming up, with the latest IMF projection indicating upward revision to the earlier growth projections for 2017-18. Global growth is now projected at 3.6 and 3.7 per cent as against the previous projections of 3.5 and 3.6 per cent for 2017 and 2018, respectively. The projection notwithstanding, a number of risk factors, ranging from economic to geo-political issues, may constrain the prospects of full recovery and the beneficial impact on emerging economies. Firstly, in spite of the expected improvement in the global economy, growth projection has been downgraded for some systematically important economies like the US and UK. Given that the US in particular accounts for over 60 per cent of Nigeria's export market, the implication of the downgrade is fairly obvious for the

external sector particularly current account balances and by extension, external reserves.

Another major issue with possible risk implication to the global financial markets is the rising level of Cryptocurrencies. Although the ratio of Bitcoin to banknotes is still small in large currency areas like the USA, the picture is completely different in other jurisdictions, even in countries within euro area. Apart from the fact that this development would diminish the ability of central banks to monitor payment system, it would also curtail their ability to control money supply and credit. In response, monetary authorities particularly in developed economies may increase interest rates as incentive for bank based payment instruments. Such a response has the tendency to increase the interest rate differentials between the advanced markets and emerging market economies thereby reinforcing capital flight from the latter. Still on the financial markets, the US Federal Open Market Committee (FOMC) concluded the November 2017 meeting by leaving the rate unchanged against widely held expectation. The statement from the Committee, however, showed that the US economy was getting stronger to accommodate higher interest rate, but the prevailing interest rate was retained primarily on political consideration, as the Committee awaits the appointment of the new FED Chairman. In essence, the agenda to increase interest rate is still much in focus.

With respect to the commodity markets, medium term projection for crude oil prices is in the range of US\$50 per barrel, which is a positive trend. This

projection, however, is underpinned by major producers production cuts and falling US crude oil inventories. In essence, inability to keep production freeze agreement, as currently being witnessed in Organisation of Petroleum Exporting Countries (OPEC), coupled with rising US crude oil production would constrain the upside for oil prices.

On geo-political front, post Brexit negotiation is still ongoing, while the tension between the North Korea and US remains elevated. With particular reference to the crisis in the North Korean Peninsula, policy makers would be extremely naïve to completely discount the possibility of physical conflict, which would adversely impact worldwide supply chains with ripples across the globe. Financial markets would be hard hit through a rise in risk premia particularly in the Emerging Asia given that the region may be temporarily destabilized by the conflict. On account of the aforementioned risk factors therefore, it is not unlikely that global capital movement may still skew in favour of the advanced economies, requiring proactive policy response from emerging economies, including Nigeria.

Domestic Environment

As pointed out above, it is noteworthy that the Federal Government is taking bold steps to confront the challenges to growth as evidenced in the allocation of about 30 per cent of 2018 budget to capital projects as well as the recent release of three executive orders. Despite these measures, some

risk factors with potential to crystalize are still visible. Some of these issues are presented below.

Oil Price and Volume Assumptions in the Fiscal 2018 Appropriation Bill: The proposed 2018 Appropriation Bill is predicated on some assumptions that appear overly optimistic. Among others, crude oil production is projected to increase to 2.3 mbd with benchmark price of US\$45 per barrel. While the projected oil price could be adjudged realistic, there is a need to recognize that the current rally in crude oil price is anchored on production cut deal particularly from OPEC members which have been largely successful. Thus, even though the assumption of production level and its impact on projected revenues in the budget may be optimistic, this will most likely be compensated by upside tendencies in oil prices. This is given that oil price has upside momentum as a testament to the successful outcome of OPEC cuts among other positive factors.

Size of Deficit in the Proposed 2018 Appropriation Bill: It is a positive development that the level of deficit in the proposed Appropriation Bill reduced to 1.77 per cent of GDP from 2.14 per cent in 2017, but the absolute size of the deficit at about two trillion naira is still very big. The fiscal deficit is to be financed, at the ratio of 50:50 per cent from domestic and external sources. Either of these sources has severe implication for macroeconomic management. However, even as the absolute level of deficit in the 2018 budget may appear to be high, this can be justified in the context of the increase in capital allocation and the tendencies to externalize the financing

of the deficits will help address the monetary policy implications of the budget and indeed improve current debt service challenges.

Delay in Budget Passage: The President has submitted the 2018 Appropriation Bill to the National Assembly for deliberation and ratification. In an ideal situation, the budget cycle should run from January to December. It is very doubtful if deliberation on the proposed budget by the National Assembly could be completed by the end of the year. This implies some kinds of delay on implementation of capital expenditure with the implication of stifling the recovery process.

Preparation towards 2019 General Elections: Another issue that may take its toll on the recovery process is likely heightening of political activities from 2018, given that it precedes 2019 when general election would be held. There is the tendency for electioneering activities to increase, which would lead to significant injection of money on recurrent expenditures. This invariably, has the tendency to cause a setback on the current downward trend on inflationary pressures, if the process is not well managed. Therefore, the liquidity threat in the context of 2018 being a pre-election year and the absolute size of the 2018 budget will no doubt be a risk to price stability that MPC must have to tackle proactively.

Way Forward

Timely Passage of the 2018 Appropriation Bill: A preliminary review of the 2017 Budget revealed that only N450 billion of the capital vote was released as at

the end of October 2017, translating to about 20 per cent performance. This is definitely below the acceptable threshold for an economy recovering from recession. From the benefit of hindsight, the reason for such poor performance is largely due to delayed commencement in budget implementation on account of late passage of the Bill into law. Given the imperative of accelerating the recovery phase, the various initiatives in the capital project should not only be executed, but the execution should equally be done speedily. As such, both the National Assembly and the executive should work together in fast-tracking the passage of the proposed Appropriation Bill.

Strengthening of Macro Stability: It is a little bit appealing to provide some forms of monetary policy support to the ongoing recovery, which makes monetary easing look as an attractive option. It is however, necessary to recognize that a significant part of the ongoing improvement is propelled by improved confidence of the key stakeholders. For example, there is a growing patronage at the Investors' and Exporters' (I&E) window of the foreign exchange market, signifying enhanced level of confidence by economic agents. As a result, the appropriate support from monetary authority at this period should be in the area of strengthening the stability in the macroeconomic environment in order to avoid time-inconsistency issue. Although inflation is decelerating but at 15.91 per cent is still high while the stability in the foreign exchange market could be threatened in the event of increase in interest rate by the Federal Reserve of the US. Given that the risk

of vulnerability is not sufficiently strong to justify increase in the policy rate, the stability in macro indicators is equally not sufficiently robust to warrant monetary easing.

Sustained Interventions in Real Sector: The recovery process is not yet inclusive. Recent data released by the National Bureau of Statistics (NBS) showed that non-oil GDP still contracted in Q3 2017. The importance of real sector in driving the ongoing recovery cannot be overemphasized. Developments in the crop subsector of the agricultural sector has been encouraging, particularly with the recent breakthrough in rice production, but the solution to the current challenges should be all inclusive, involving the entire agricultural value chain. The challenge of recovery in the real sector is further compounded by weak support from the banking system. For example, credit to the private sector contracted by 0.24 per cent in October, annualizing to a contraction of 0.28 per cent, against a growth target of 14.88 per cent. Given the magnitude of expected borrowing by the fiscal authority in 2018 Appropriation Bill, private sector credit from the banking system would not only slowdown, but the pricing would equally be inconsistent with viability of the real sector. As such, the Bank should continue to strengthen its various intervention measures like the Anchor Borrowers Programme and NIRSAL with a view to driving activities in the real sector.

Decision

In the light of the fact that the improvement in the macroeconomic environment is yet to firm up coupled with pockets of likely risks particularly from the global environment, I would like to vote for the retention of all the existing measures of monetary policy.

4. GARBA, ABDUL-GANIYU

Decision

1. My vote is similar to the one I offered in my September 2017 personal statement except that instead of a 50 basis point rate cut, I vote to reduce the MPR by 100 basis points (1%). This implies (i) a reduction in the MPR from 14% to 13% and (ii) a reduction in Standing Lending Facility (SLF) from 16% to 15% and the Standing Deposit Facility (SDF) from 9% to 8%.
2. My vote is still a vote for (i) consistency and effectiveness of monetary policy; (ii) growth in private investment, creation of new jobs, output growth, financial system stability and medium term macroeconomic stability; (iii) a shift from passive monetary policy (Hong Kong Model) to an active and truly independent monetary policy (Chinese Model); (iv) substantive medium term macroeconomic stability rather than a superficial (whited sepulcher-type) short-term stability and (v) a gradualist approach to the shift from passive to active monetary policy regime.

Justification

3. My justification is also similar to the one in my September 2017 personal statement. I will therefore provide highlights of my justification and re-emphasize the requirements urgently moving along the three interrelated strategic and policy pathways: low inflation conducive to growth, financial system stability (FSS) and fiscal prudence or discipline.

4. Because this is the last MPC of 2017, I will start with a brief evaluation of the policy environment compared to this time last year. The evaluation and the outlook for 2018 give further context to my vote.

A Brief Review

Year 2016 was a very difficult year for monetary policy, fiscal policy, financial markets, the macro-economy and the well-being of Nigerians. The economy was technically in recession in the second quarter of 2016 and persisted through the first quarter of 2017. However, the economy had been slowing down since 2014. The headline, food and core inflation rates rose sharply by 93%, 64% and 103% in 2016 compared to much smaller growth of 20%, 15% and 44%, respectively in 2015. Money supply (M1) was expanded from ₦6.9 trillion in December 2014 to ₦8.6 trillion in December 2015 and to ₦11.3trillion in 2016. This means that money supply rose by ₦4.4 trillion between December 2014 and December 2016: a phenomenal growth of 64% within 24 months! In the same period, Headline, food and core inflation rose by 131%, 90% and 131% respectively. A plot of inflation and M1 show a strong tracking of inflation path by the path of money supply in the 24 months between December 2014 and December 2016. The rate of expansion in M1 between 2014 and 2016 points strongly to a strong discordance between the restrictive monetary policy regime of the period and the growth of monetary supply. The main driver of M1 growth is "Central bank demand deposit" which rose from ₦217.05 million in December 2014 to ₦3.25 trillion in December 2016. This

level of liquidity injection did not justify the increases in MPR and short term interest rates. Neither did it help the goals of price stability, stable exchange rates, investment and output growth or reduction in unemployment. The high growth in inflation to more than twice the upper bound of 9%; the loss of international value of the naira, the high spread of ₦150/\$ depreciation, the recession, the rising unemployment and the incredible growth in public debt are not independent of the revolving door of liquidity injections and liquidity mop-ups.

As I emphasized in previous personal statements, such expansionary growth in money supply are not compatible with a restrictive monetary policy regime or with its associated high interest rates, prohibitive costs of liquidity management or adverse effects on fiscal policy. Between the fourth quarters of 2014 and 2016, respectively, total public debt stock rose by ₦6.64 trillion from ₦7.90 trillion. The fiscal problem posed by such phenomenal growth in public debt is beyond the issue of crowding-out to a question of sustainability because at this rate of growth of public debt and the high interest rates, public revenue will not be enough to pay for debt service.

In the first ten months of 2017, the economy exited technically from recession. Any excite however, is premature. First, the economy is far from its level in third quarter of 2015 and is yet to match the growth rates before growth slowed down. What is more fundamental is that the celebrated growth in the third quarter of 2017 of 1.4% was due mainly to growth in oil GDP (2.09%). Despite the growth in Agriculture (0.88%) driven by harvests of crops; non-oil

GDP contracted by -0.76% with services (-1.02%), trade (-0.29%) and manufacturing (-0.26%) the lagging sectors. A clear headed analysis would indicate that by excluding the oil and gas, the economy was back to negative growth from the 0.72% in first quarter and 0.45% in the second quarter of 2017. Furthermore, though employment data are not available, it is safe to infer that the upward trend of unemployment from first quarter of 2015 will continue into 2017 and that current unemployment rate will exceed 14.2% and that the most active population aged 15-40 years will account for a disproportionately higher share of the unemployed.

The stock market has rebounded from the lows of 2016, when All Share Index (ASI) shed 6.2% and market capitalization declined by 6.1%. In the 10 months of 2017, ASI rose by 36.5% and market capitalization by 37.3% or ₦3.45 trillion. It is worthy of note that the stock market is in its third bubble since 2006: 2006-2008; 2012-2014 and from April 2017. The growth in the stock market were not driven by economic fundamentals, but by policies that attracted portfolio flows and, by the inflows of portfolio flows. The high yields offered portfolio investors and a relatively stable exchange rate at less than half its international price at the end of 2014 offered portfolio investors a riskless and high return investment option that was hard to resist. As a result, portfolio flows began to rise from April 2017: from \$57.5 million in March to \$119 million in April and steadily to \$1.32 billion in September.

The fiscal operations is characterized by an abnormally significant growing fiscal deficits and public debts. In the first three quarters of 2017, the public

debt was 77% higher than it was last year, when it was about ₦1.512 trillion. In the same period, public debt rose by ₦2.65 trillion or 18.2% in just 9 months! The growth in public debt in the first nine months of 2017 is already 114.2% of the total borrowing plans for 2017 and 112.2% of projected deficits for 2017. The high and unusually generous interest rates used to attract portfolio flows into treasury bills, treasury bonds and FGN bonds auctions are causal to the growth of public debt stock and money supply, which tend to exert crowding-out effects on credit to the real private sector and to public spending on social and economic infrastructures. Every y naira of new public debt at x interest rate grows the public debt by $y*(1+x)^n$. The higher the values of y and x and n the higher the public debt and money supply. For every y Naira of public borrowing, public debt grows by $x*y$. Keeping x high (via restrictive monetary policy) and y high (through lax fiscal spending), causes the public debt to grow at the risk of fiscal unsustainability, financial system instability, negative growth and high unemployment especially when the employment and output elasticities of government expenditure are very low. Clearly therefore, restrictive monetary policy and lax fiscal policy are great threats to effective and efficient macroeconomic management.

In the same period (January to September, 2017), the Federal government spent ₦1.24 trillion to service domestic debt. With a growing appetite for external debt developing in complete disregard to the experience of 1978-2006 and the costly road shows and financial service costs, the growth of both public debt and public debt service next year would most likely exceed

that of 2017. It is thus obvious that the fiscal challenges are extending beyond the usual crowding-out effects to a problem of fiscal unsustainability: a point where revenue may not be sufficient to pay debt commitments.

In my outlook for 2017 in my January MPC personal statement I wrote: “Year 2017 will be **very challenging for macroeconomic management globally and for global markets because of heightened uncertainties due mainly to political and associated economic risks.** . . . The domestic outlook indicated by the fiscal deficit, the structure of expenditure, revenue shortfalls, high levels of public debts and the crowding-out effects of public debt service and public borrowing on private sector investments and current account deficits make for **a difficult 2017.** The challenges of sourcing credit within and outside the Nigerian economy may exert pressures on the growth in money supply. Yet, as 2015 and 2016 clearly show, **it would be damaging for the credibility of monetary and fiscal policy to allow M1 match the growth of previous years.** It would significantly damage the purchasing power of the naira domestically and internationally and destabilize the economy. There is also, the challenge of twin deficits (fiscal and current account) and ensuring financial system stability to contend with.” Indeed, as the review suggests, despite the **positives** (slower growth in M1, rise in price of crude oil, managed stability in the exchange rate, decline in headline inflation caused mainly by fall in core inflation), 2017 was a difficult year for Nigeria. The costs of creating an enabling environment to attract portfolio flows is unlikely to justify the benefits of portfolio flows at least in the medium term. Two previous episodes of

capital market bubbles (2006-2008 and 2012-2014) triggered by capital account liberalization and portfolio flows had devastating effects on the capital market, money market, external account, forex reserves, exchange stability, inflation, investment, public debt, public deficits and structure of public expenditure. The game of attracting portfolio is a very risky gamble as it was in 2006-2008 and 2011-2014.

Outlook for 2018

Bank staff suggest that inflation is likely to trend downward and the exchange rate would be stable provided that oil output and prices rise, the Investment and Export window remains stable and portfolio investors continue to pour their capital into Nigeria. The perennial challenges (crowding-out of the private sector, growing costs of liquidity management, low financial intermediation and so on) are likely to persist.

Political activity will dominate 2018 as we count down to the 2019 elections. Politics tend to correlate positively with money supply and exchange rate and inflationary pressures. Thus the political premium is likely to be positive and significant. With the balance sheet normalization plans of the US Fed well underway and inflationary pressures expected to rise significantly in 2018, the economic premium is also likely to rise. Hence, the risk of capital reversal is very high. A macroeconomic management strategy hinged on portfolio flows is badly flawed. Two major episodes of portfolio flows related bubbles have provided more than sufficient empirical evidence about its destructive

payloads. I can hardly find any reasonable empirical support for a strategic support for a third capital market bubble in just over a decade!

The combinations of heightening political and economic risks dooms a monetary policy pivoted on attracting portfolio flows in 2018. It has been suggested that cutting the MPR now is premature because the inflation rate is still high at 15.91%. The fact however, is that the link between MPR and inflation broke down with the introduction of Hong Kong Model: capital account liberalization and exchange rate stabilization. Proof: at the onset of restrictive monetary policy in September 2010, headline inflation was 13.6% (August 2010) while MPR was 6%. In 2012, MPC fixed the target headline inflation band with 6% as the lower bound and 9% as the upper bound. By the time headline inflation fell within the band in January 2013, the MPR was stable at 12%, a rate that was fixed at the emergency MPC Meeting of October 2011. For 29 months (January 2013 to May 2015) headline inflation did not exceed 9% yet, in November 2014, MPR was increased to 13%. The increase was a response to pressures on the exchange rate and was in defense of the exchange rate. Practice and theory both affirm that a passive monetary policy in a small open commodity dependent economy with capital account liberalization and fixed exchange rates surrenders active and independent monetary policy. The resulting passive monetary policy not only helped handicapp the economy, it is more likely to undermine the economy through high interest rates required to keep portfolio investors excited. The fear of capital flight locks policy to a high interest rate regime.

Yet, what portfolio investors provide are whited sepulchers for reserves; and exchange rate; and the capital market. Sooner rather than later, the white paint wears off and the truth about the sepulcher becomes very obvious. I cannot support a temporary coat of paint that will sooner wash away by the political and economic realities of 2018 and beyond.

What has not changed

1. My conviction about the importance of urgently finding sustainable paths to low inflation growth conducive to job creation and economic growth, financial system stability and fiscal prudence are the most urgent strategic and policy priorities building on the “March MPC Retreat”. “Can two walk (and work) together unless they are agreed” (Amos 3:3). The answer is a resounding no! A person with two legs will be foolish to walk only on one leg. He/she will also be foolish to set the two legs in competition with each other causing them to constantly disagree about which directions to go.
2. The foundations of the March Retreat in the following three key area remain fundamental: (i) the relationship principles of humility, sincerity and integrity; (ii) the organic links between fiscal, monetary and prudential policy and the urgent necessity for interdependent and coordinated strategic and policy analysis, choices and actions and (iii) the urgent need for coordinated and effective movements along the three pathways: low inflation conducive to growth, financial system stability (FSS) and fiscal prudence or discipline.

3. The growing costs of ignoring the lessons of Nigerian and global economic history to the present and the future of Nigeria. Failure to learn from mistakes
4. The macroeconomic challenge remains overwhelming: (a) a tentative exit from technical recession driven by oil GDP – a long way from recovery to 2014 level let alone growth from 2014 level; (b) an unemployment rate of 14.2% as at 2016:Q4 (likely to be higher given the trend); (c) a 0.04% fall in headline inflation driven by seasonal effects, which caused a decline in food inflation of 0.03%, partly offset a 0.1% rise in core inflation; (d) a ₦2.01 trillion rise in public debt, a Federal deficit of ₦1.9 trillion in the first 8 months, debt service of ₦1.58 trillion (2.4 times the spending on capital project); (e) rising maximum lending rate to 31.2% (by 0.26%) and prime lending rates of 17.69% (by 0.04%) and widening interest rate spread to 26.95% (from 26.83%); (f) a very active revolving door of liquidity – pumping in and mopping out; (f) collapse of the interest rate corridors which makes Standing Lending Facility and Standing Deposit Facility rates redundant as effective monetary policy tools; (g) 32.1% growth in All Share Index driven mainly by banking stocks (58.6%) and Consumer Goods (31.81%) that are in turn powered by (h) a monthly average growth in portfolio and FDI investments in the capital market that averaged 52% between April and August 2017.
5. **The unresolved issues:** (a) a forward looking medium to long term strategic macroeconomic management framework for Nigeria as the

context for policy analysis and choice; (b) continuing malfunctions in the credit market which tends to allocate credit to sectors with traditionally high NPLs and low output and employment elasticities as well as a tendency to restrict access and to charge maximum rates on credit to sectors and economic agents with traditionally lower NPLs and higher output and employment elasticities; (c) the dominance of rent havens in both the real and financial sectors, and the public space; (d) prevalence of present hedonistic and backward looking orientation and (e) inefficient and ineffective use of existing Nigerian capacity in all aspect of the political economy.

6. The **Hong Kong model** within which monetary policy has been conducted since January 2012, which uses high interest rates to attract portfolio flows while hurting domestic investment, growth, employment and expanding public debt and money supply and distorting the structure of public expenditure and reducing its output and employment elasticities of public spending. The case against reducing interest rates has less to do with the inflation rate than with fears about possible reversal of portfolio flows. The questions we must answer include: which is best for growth and employment: portfolio flows or domestic investment? Is portfolio flow more stable and heavier than remittances? Does portfolio flows have higher employment and growth elasticities than remittances? If the answer to the questions is a resounding no, a strategic policy overhaul is imperative.

7. My preference for **the Chinese model as a better option to the Hong Kong model**. I still believe that the Chinese model limits vulnerability to destabilizing financial flows and frees monetary policy to support growth, employment, financial system stability and lower fiscal imbalance.

Finally

8. My vote is still for a gradualist approach in a shift from an **outward-oriented passive** monetary policy to an **inward-oriented independent** monetary policy.
9. A 100 basis cut in MPR is still, just a first step on the paths to low inflation conducive to growth, financial system stability and fiscal prudence. It should be a consensus point on which the monetary and fiscal authorities could build on to produce a consistent forward looking strategic framework for coordinated, effective and constrained monetary, prudential and fiscal policies.

5. NNANNA, OKWU JOSEPH

Nigeria's growth remains positive despite its seeming fragility thanks to the uptick in oil prices and improved oil production. Real GDP grew by 1.4% in Q3 of 2017 up from 0.7 per cent in Q2 and Q1 contraction of 0.91 per cent. The major drivers of real GDP growth were agriculture (0.88%) and industry (1.83%). The Manufacturing Purchasing Managers Index (PMI), which stood at 55.0 index points in October 2017, indicated expansion in the manufacturing sector. Similarly, the composite PMI for the non-manufacturing sector stood at 55.3 index points in October 2017, indicating growth for the sixth consecutive month. However, structural headwinds remain a drag to growth in the non-oil sectors as the manufacturing and construction industries continue to be constrained by power supply shortages. Consequently, non-oil real GDP contracted by 0.76 per cent in Q3 2017.

Inflationary pressures are receding reflecting the contraction in money supply and the relative stability of the naira exchange rate. Headline inflation (year-on-year) decelerated albeit marginally for the ninth consecutive month to 15.91 per cent in October 2017 from 15.98 per cent in September 2017. Food inflation which stood at 20.31 per cent remained elevated due to distribution bottlenecks, high prices of farm inputs and supply shortages as a result of increased cross border sales. Core inflation increased slightly to 12.14 per cent from 12.12 per cent in the same period.

Though structural constraints have continued to impede transmission of credit to the real sector, liquidity conditions and investor sentiments remain positive.

Net liquidity positions and flows reflected the effects of Federation Account payments to states and local governments; remittances by the Nigerian Customs, Federal Inland Revenue Services; OMO sales; foreign exchange interventions and maturing CBN Bills. Reflecting banking system liquidity, the average inter-bank call rate, which opened at 12.00 per cent on October 3, 2017, closed at 5.38 per cent on November 16, 2017. The OBB rates opened at 10.41 per cent and closed lower at 6.02 per cent in the same period. However, the average inter-bank call and OBB rates for the period stood at 10.94 and 10.15 per cent, respectively. Credit to the private sector fell by 0.24 per cent in October 2017, while net credit to government rose by 7.60 per cent. The All-Share Index (ASI) rose by 3.38 per cent on November 17 from 35,504.62 on August 31, 2017. Market Capitalization (MC) improved by 4.35 per cent to ₦12.77 trillion from ₦12.24 trillion during the same period. Banking industry profitability improved significantly, although I am not under any illusion that the challenging macroeconomic environment could have adverse effect on non-performing loans (NPLs).

Global economic activity is improving albeit widening imbalances. Global output is projected to improve to 3.6 per cent in 2017 from 3.2 per cent in 2016 reflecting the recovery in oil and other commodity prices. Growth in the advanced economies is projected to increase to 2.2 per cent in 2017 from 1.7

per cent in 2016. Similarly, emerging markets and developing economies are forecast to grow at 4.6 per cent in 2017 up from 4.3 per cent in 2016. I note that the global outlook for growth is beclouded by the prolonged tension in the Korean Peninsula, potential *BREXIT-cliff* and financial market uncertainties due to monetary policy normalization in the US.

Fiscal space to implement the 2017 budget into Q1 of 2018 remained delicate in the absence of strong buffers. However, more revenue was expected from achieving and sustaining oil production at 2.2 mbpd. The tailwinds will be the continued implementation of the 2017 budget into early 2018, anticipated improvements in government revenue from the implementation of the Voluntary Asset and Income Declaration Scheme (VAIDS) and favourable crude oil prices.

External sector indicators remained resilient, supported by improved oil production and sustained foreign exchange market liquidity. Gradual organic convergence of the rates at the bureau-de-change (BDC) and the Nigeria Autonomous Foreign Exchange (NAFEX) market segments is evident. Clearly, there is stability of the exchange rate at the inter-bank foreign exchange market since the last MPC. The Investors' and Exporters' (I&E) window had increased liquidity and boosted confidence in the market with over US\$18.70 billion in total transactions since its introduction in April 2017.

Overall, staff estimates indicate positive macroeconomic outlook for the economy up to Q1 2018. I note the development financing initiatives of the CBN, particularly, in agriculture; the resolute implementation of the 2017 budget; and the speedy passage of the 2018 budget as essential to output expansion and job creation. Hence, I vote to retain the current stance of monetary policy tightening.

6. UCHE, CHIBUIKE U

Perhaps the only positive economic development in Nigeria since the last MPC meeting in September 2017 is that global oil prices have continued to inch upwards. Despite this, the economic future of Nigeria remains bleak. Based on the figures contained in the President's 2018 budget speech, for instance, it is obvious that the fiscal authorities still have not mustered the political will necessary to curtail the embarrassingly high government recurrent expenditure. The continued maintenance of an over bloated civil service at the expense of the much needed basic infrastructure for the development of the private sector and for the promotion of sustainable economic growth makes no sense.

As I have pointed out in previous statements, I am particularly disturbed by the recklessness with which the Federal Government has been borrowing, both internationally and locally. It is obvious to me that very little consideration has been given to how these loans would be repaid in the future. With the medium to long term expectation that oil will become less important in the global economy, it is nothing more than wishful thinking to expect that these new loans will be repaid from oil cash flows in the future.

The absence of a clear and robust economic plan and/ or strategy on the part of the Federal Government has continued to impact negatively on the monetary policy terrain in the country. The ability of the CBN to ensure monetary and price stability has been greatly impeded under the above

circumstances. I am of course aware that our national reserves have been inching upwards for some time now. I am however not convinced by the argument that the rising reserves is evidence of good monetary policy management by the CBN. This is because I have consistently argued that allowing short term portfolio inflows into the country and then using such proceeds to fund imports and consumption makes little sense. All that such a policy can do is help to temporarily sustain the foreign exchange cash flow of the country while driving it deeper into international debt.

This is not sustainable as there is a 100% certainty that the bubble will burst. Few will, for instance, dispute the fact that the most probable outcome of the scenario where the cost of capital is higher than the return on investment is economic doom. While it is true that such temporary inflows could help sustain the value of the local currency, this kind of relief can only be temporary. What gives permanent relief is the expansion of the underlying economy and exports. Unfortunately, this has been hampered in Nigeria by poor infrastructure and poor governance.

In the context of the peculiarities of Nigeria, the temptation to turn the CBN into a *Santa Claus* for the Government should also be resisted. This is because it destroys the balance sheet of the CBN and complicates its monetary policy management function. It, for instance, makes no sense for the CBN to create liquidity problems (by printing and spending huge amounts of money on behalf

of government) and then go ahead to spend equally huge amounts of money trying to solve the problem it created (mopping up the liquidity).

The poor economic policy choices of Government are not only endangering businesses, they are also endangering the financial system. I find it very troubling that less than a decade after Nigeria emerged from one of the worst financial crisis in its history, it is gradually inching towards another one. This is even more so given the fact that the massive financial hole created in the attempt to address the last crisis (AMCON) is yet to be meaningfully resolved. It is instructive that the current aggregate bad debt levels of Nigerian banks are now in double digit territory and still rising.

Inflation also remains in double digit territory and is still above MPR. It is in the light of the above that I find calls for MPR to be lowered rather frustrating. On the other hand, increasing the MPR will further increase the interest rates of banks and subsequently, the nonperforming loans of such banks. It is in the light of the above manmade difficulties that I have come to the careful conclusion that the least destructive policy path for MPC will be to do nothing.

I therefore vote as follows: (i) to retain the MPR at 14.00 per cent; (ii) to retain the CRR at 22.50 per cent; (iii) to retain the Liquidity Ratio at 30.00 per cent; and (iv) to retain the Asymmetric Window at +200 and -500 basis points around the MPR.

7. YAHAYA, SHEHU

I vote to maintain the current monetary stance, due to the reasons provided below

Developments in the Global Economy

The year is coming to an end with some positive global economic developments. Global output is expected to improve this year with compared with 2016. Although GDP growth rates for the US experienced a minor blip in Q32017 as compared to Q2 results, the growth rate for 2017, expected at around 2.2% will be appreciably higher than in 2016. Both the Euro area and the UK experienced positive growth in Q3. GDP growth rate in China has remained fairly stable and is expected to be slighter higher than last year, while there was a slow- down in Japan, even though growth remained positive. There is expected to be a substantial economic recovery in Sub-saharan Africa. South Africa regained a positive growth rate in the last quarter. Generally speaking, despite concerns about the slow-down in China and the UK, there are strong prospects for a more robust global economy in 2018.

Oil prices have been relatively buoyant, with Bonny light above \$50/b during the second half of 2017, reaching over \$60/b last week, compared to an average of less than \$40/b in 2016. As oil prices rise however, it is certain that output, particularly from shale oil producers, will rise, thereby raising global supply and undercutting prices. Despite the political and security challenges

facing a number of major oil producing countries, the medium-term prospects for oil prices therefore remain uncertain.

Another important development has to do with global interest rates, or at least interest rates in some of the major economies in the world. The US Federal Reserve policy rates are on a trend towards normalization, with strong prospects for a series of interest rate hikes in the next year. The Bank of England has recently hiked its rate and the EU, while continuing with its quantitative easing program, is also doing so at a reduced pace. Higher interest rates in these countries and regions would obviously pose challenges to developing economies by pulling some or much of international investments from them, making debt service more difficult, and exerting additional pressure on their currency exchange rates.

The Domestic Economy

GDP grew in Q3 of 2017 by an estimated 1.4%, doubling the figure of 0.7% for Q2, the highest achieved since 2015. The sub-narrative however is that the non-oil sector has been experiencing a decline fell by 0.76% during Q3. Solid minerals had remained flat and the manufacturing sector showed a negative growth of -0.26. Construction, Trade and services all declined. The agricultural sector, mainly buoyed by crop production, has however maintained a trend towards recovery, although at a slower pace than expected. The impetus for growth was therefore mainly from a recovery in the oil sector, which grew by

2.09% during the quarter, due to both improved output and higher price levels compared to 2016 and the first half of 2017.

The slow downward trend for headline inflation continued during October with the price level at 15.91%, mainly due to a slight decline in food inflation, driven by a slight decrease in the rate of increase of prices of farm produce. Otherwise most other items in the basket remained flat, at about the same level as in September 2017, except for imported rice, which experienced an increase. Overall, food inflation remained high at 20.31%. Core inflation inched up in October 2017, year-on-year, mainly due to the slight increase in prices in the transport, housing and utilities sub-sectors. Month-on-month, it dipped slightly.

The level of foreign reserves continues to build, reaching approximately \$34.92 billion by mid- November and should reach \$38b by December 2017. This has been possible due to a combination of policy initiatives, such as the exporters and investors window which has encouraged a surge of Foreign Portfolio Investment (FPI), external borrowing and an improvement in oil earnings. Non-oil exports have accounted for only slightly higher than 1% of inflows between August and September this year. The build up of reserves in turn has helped to maintain stability in the foreign exchange market, narrowing the gap between Bureau de Change (BDC) and inter-bank rates. Nevertheless, there are significant risks involved here, since a substantial proportion of the foreign investments are in the form portfolio investments (accounting for about two-thirds of capital inflows in October 2017), which

are rapidly reversible, and a much smaller proportion in the form of FDI. The capital market has clearly benefited from the surge of portfolio investment, with the ASI rising more than 36% in the course of 2017.

The banking and financial sector of the economy is basically sound, although facing some significant challenges. It presents a complex and sometimes puzzling picture, whereas DMBs profits have increased by more than 60% in the last one year, mainly driven by increases in interest income; return on equity (ROE) and return on assets (ROA) are showing an upward trend and are higher than comparator countries; Yet total credit to the economy decreased by a little over 3%; non-performing loans (NPLs) are rising and the capital adequacy ratio, while still above the regulatory threshold, is declining. One positive development though was that, by October 2017, the Agricultural sector accounted for 13% of new credits. Clearly the various efforts made at encouraging support for this sector are bearing some fruit. Moreover, NPLs are concentrated in a few sectors that have borne the brunt of the economic recession and the extent of provisioning for bad loans has been raised sufficiently to cover the risks. Concentration risks and issues around Net Open positions still need to be tackled, while vulnerability to exchange rate risks have abated somewhat.

External borrowing also has some challenges. It is eminently sensible to significantly increase investments in the economy in order to climb out of recession. Also, some substitution between domestic and foreign borrowing may reduce the burden of debt service as well as crowd in private borrowing

and even help reduce domestic interest rates. However, the debt service/government revenue ratio is a particularly critical measure in an economy where the tax/GDP is so low. This is however getting so high that sustainability may become an issue, particularly in the medium term. If tax revenue does not rise significantly, debt service may undermine the capacity to finance capital expenditure. Moreover, the assumptions behind increased external borrowing may be substantially affected by increases in global interest rates and pressures on the naira exchange rate. This calls for greater caution.

It seems that the scope for substantially expanding domestic revenue mobilization has not been exhausted. The various policies aimed at extending the tax net are quite positive. It is hoped that these will yield better results in 2018. However, financing deficits through the sale of government assets needs to be carefully considered, as there are options that may yield a more regular revenue stream and avoid some of the political economy risks of outright sales (including worsening income distribution). These options could include raising financing through securitization and collateralisation of the appropriate assets.

As indicated above, much of the recovery observed during Q32017 is attributable to recovery of prices and output in the Nigerian oil sector. The stability in the exchange rate is due to CBN interventions in the market and other active policies, as well as the substantial increase in foreign reserves. These interventions and many of the policy initiatives have been made

possible by the increase in earnings from oil and external borrowing. Government revenue also needs to pick up to galvanise the fiscal impetus to growth. There is some progress in the agricultural sector: certainly, there is evidence of a substantial reduction in primary food imports. The increased government focus on capital expenditure is very positive and more creativity is needed to effectively fund the growth-enhancing programs. In general, therefore, there is still much to be done to sustain many of the policy initiatives and to embark on additional ones in order to maintain the recovery impetus and to raise the GDP growth rate above the population growth rate and to achieve the goals of restructuring the economy

As far as monetary policy is concerned, it appears that the imperative is to continue to build reserves, maintain exchange rate stability which should help to resuscitate manufacturing output. CBN and government programs are also required to address funding gaps in the agriculture sector, since this cannot at this time, be largely met by DMBs, despite the significant increase in new loans to this sector. Combined with the strong focus on infrastructure development, this will help under-cut supply-side inflationary pressures. In the medium term, it would then be possible to focus attention on reducing interest rates.

For the short term, MPR cannot be substantially reduced since inflation is only falling slightly and is still too high. Moreover, some of the factors that are exerting a downward pressure on price levels such as the very low level of monetary aggregates- both M1 and M2 are contracting, credit to both

government and the private sector are below the designated benchmarks- cannot be expected to continue at their current sub-optimal levels. Global price levels are also likely to go up a bit in the course of 2018, thereby contributing to imported inflation.

Under the circumstances, I vote to maintain the current monetary policy stance

**8. EMEFIELE, I. GODWIN, GOVERNOR OF THE CENTRAL BANK OF NIGERIA
AND CHAIRMAN, MONETARY POLICY COMMITTEE**

Over the course of the year, key macroeconomic indicators have continued to improve as recovery consolidated in the third quarter of 2017. Real GDP growth improved from a contraction of 0.9 per cent in 2017q1 to expansion of 0.7 and 1.4 per cent in quarters two and three, respectively. Inflation rate maintained a steady decline from 18.7 per cent in January 2017 to 15.9 per cent in October 2017. The exchange rate in the various foreign exchange market segments remained stable and are converging towards NGN360/US\$ as external reserves had risen to US\$34.8 billion at November 20, 2017. Our balance of payments account strengthened likewise with surpluses in the current account balances. These outcomes portend a brightening outlook for the Nigerian economy in the near- to short-term with a projected real growth of 0.8–1.0 per cent for 2017 from -1.6 per cent in 2016.

Global growth for 2017, according to the IMF, is projected at 3.6 per cent vis-à-vis 3.2 per cent in 2016 due to recoveries in oil and commodity prices. The projections for advanced economies indicated a growth of 2.2 per cent in 2017 from 1.7 per cent in 2016, while emerging market economies are expected to grow by 4.6 per cent in 2017 compared with 4.3 per cent in 2016. For sub-Saharan Africa, growth rate is projected to rise from 1.4 per cent in 2016 to 2.6 per cent in 2017. The upward revisions in these forecasts suggest improving prospects of global demand which could act as a tailwind to the

continued recovery of the Nigerian economy in short-term. However, the heightened tension in the Korean Peninsula, intricate BREXIT negotiations and financial market vulnerabilities could impinge the domestic economy in the short-to medium-term. This risk is further complicated, in the long-run, by the ramifications of the unpredictability of oil prices on our economy, which still relies on oil export for much of government revenue.

Against this backdrop, the call for diversification of the Nigerian economy remains sacrosanct. I note that although the rise in real GDP growth rate is heartening, it is below the population growth rate. Besides, the slowdown in non-oil GDP in 2017q3, the falling per capita income and the high rate of unemployment remain going concerns amidst the positive metrics recorded so far in the year. It is imperative to ensure that monetary, fiscal, and structural policies are synchronised and delicately balanced in order to achieve a thriving well-diversified economy with low inflation and unemployment rates.

I note the boost in investor confidence and business sentiment following the continued recovery of the economy. Conjointly with the increased stability in the foreign exchange (FX) market, this had a positive spill-over effect on the domestic capital market performance as reflected in the 36.6 per cent and 38.1 per cent year-to-date growth in the all share index and market capitalisation, respectively. Money market conditions, however, remained tight during the review period. Broad money supply showed an annualised contraction of 5.5 per cent in October 2017 in contrast to a target expansion

of 10.3 per cent. Analysis of the domestic credit analogously indicated an annualised contraction of 0.3 per cent in private sector credit vis-à-vis the benchmarked growth of 14.9 per cent and in contrast to the 9.1 per cent annualised expansion of net claims on government. In this regards, I note the apathy of banks to lend to the real sector especially in view of the elevated credit risks resultant from fragile macroeconomic conditions and the attractive yield on risk-free securities. The CBN will continue to work with banks to ensure that low-priced credits are sufficiently channelled to high impact sectors with a view to bolstering domestic productivity, creating jobs and reducing poverty.

Overall, I note that the recovery of the economy is strengthening as key indicators consolidate; although, it remained structurally delicate, especially given the contraction of the non-oil sector in 2017q3. I reiterate that the stability in the FX market remains a significant factor in the macroeconomic improvements that have been recorded. To safeguard the ongoing recovery, it is necessary to ensure that gains from the relative FX stability are not derailed. We must maintain a balanced inflow of foreign capital to the economy by always ensuring appropriate interest rate parity. The desire for an accelerated recovery must be properly balanced with the imperatives of price and exchange rate stability. In this regard, the CBN will continue its interventions in critical sectors of the economy so as to support the government's efforts at bolstering domestic productivity. I re-emphasise the need to sustain the pace of capital projects in order to reduce infrastructural

deficits, boost output and moderate prices. I am of the view that, if judiciously implemented, the 2018 budget of the fiscal authorities and the proposed capital expenditure therein will have a significant push effect on the real economy.

I reiterate the need for cautious policy decisions. While the path of inflation is pleasing, its level is yet unacceptable. In my consideration, I note that a balanced analysis of options is most essential. A decision to ease monetary stance in order to accelerate GDP growth may reverse recent disinflation and worsen the already intolerable level of inflation. On the other hand, further tightening at this time may strangle the emergent recovery and exacerbate the already depressed demand of household and private businesses. It is important to emphasise that the current inflation rate, at 15.9 per cent, remains at a growth inhibiting level. Hence, the need to retain the restrictive stance of policy without further tightening. I am of the view that the current level of real interest rate is appropriate to balance the objectives of exchange rate stability, price stability and output stabilisation.

I remain personally in favour of low nominal interest rate in the long-run. Nonetheless, a drive to force down interest rate would be counterproductive at this time. It is important to avoid impulsive policy shocks, which could reverse ongoing disinflation, upend the path of recovery and destabilise FX market. Consequently, I vote to:

1. Retain the MPR at 14.0 per cent;
2. Retain the CRR at 22.5 per cent;
3. Retain the asymmetric corridor at +200/–500 basis points; and
4. Retain liquidity ratio at 30.0 per cent

Godwin I. Emefiele, CON
Governor

November 2017