FDC Economic Bulletin

September 26, 2017

CBN Holds Again – Better Safe than Sorry

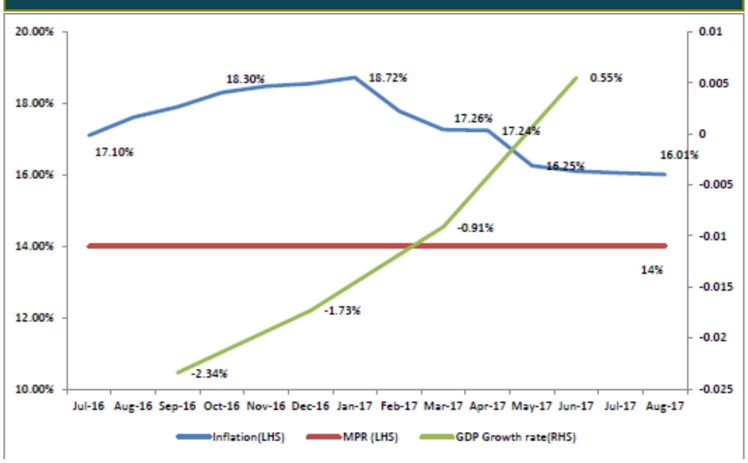
In line with market consensus, the MPC kept monetary policy stance on hold and maintained status quo on other parameters. This decision enables the central bank to buy more time to see if the current growth momentum and the inflation reduction are sustainable. Of the seven members, only one voted for a reduction in interest rates.

Committee's Considerations

The fundamental argument behind maintaining the status quo for the 7th consecutive meeting is the fear of the fragility of the exchange rate, inflation and GDP growth. Its major focus remains maintaining price stability and preserving the value of the naira. The CBN has consistently relied on the feedback monetary policy rule i.e. it has been reactive rather than proactive in seeing itself as a stimulant for economic recovery.

The considerations also included positive growth in the developed and emerging markets and an overall improvement in global macroeconomic conditions.

Chart 1: Headline Inflation vs Month-on-Month Inflation (%)



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[1] NBS, FDC Think Tank

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Rationale

The CBN reiterated its commitment to policy flexibility in the near time despite maintaining the status quo on policy rates. This implies that there is the possibility of a change in policy stance at its next meeting in November. The MPC had no reservations about the need for time to evaluate the versatility and robustness of its policy position. It alluded to the difference between inflation data and expectations and was definitely not convinced that inflation expectations were subdued enough to enable the CBN inject more liquidity into the system. It noted that in spite of the contraction in M2 (-11.06% annualized) and tepid extension of credit to the private sector, inflation was still way above the CBN's comfort zone. Therefore, in summary, the central bank put caution above audacity, and wisdom above courage in arriving at the better safe than sorry approach.

Peer Comparison

Compared to global and regional countries, the central bank accepted that Brazil, South Africa and Nigeria exited a recession, whilst growth projections in the European Union, Britain and the US were positive. Its decision is similar to that of Ghana, South Africa and Kenya.

Outlook

The MPC de-emphasized the fact that oil prices are at a 26-month high and that production at 1.8mbpd can guarantee enough supply into the forex market. The immediate impact of this decision is that naira liquidity will be tight, credit growth will be squeezed and the stock market will witness a decline in prices in the short run.

Therefore, we believe with external reserves at $32.9bn as of September 25th and inflows of $7bn in 5 months at the IEFX window, the CBN has no reason not to pursue an accommodative slant in its open market operations between now and its next meeting in November.