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NIGERIA RESEARCH NOTE [REV.]

The March 2016 MPC - monetary policy planted firmly in mid-air

*In retrospect, the omens for this month's session of the MPC were inauspicious from the outset. In the first place, the meeting was taking place only a week after news broke of the **CBN having fallen victim to a classic '419' fraud, leading to the suspension of the Deputy Governor for financial system surveillance**[1].*

*Worse still, the session was **convening in the shadow of the National Economic Council's own two-day meeting**, at which President Buhari's opening address included a number of prescriptions that were not only heterodox, but **significantly infringed upon the CBN's notional independence**, most notably:*

- *Banks should be leaned upon to substantially increase their lending to the agricultural sector. **CBN should bear part of the risk of such loans as a matter of national policy** (sic).*
- ***CBN should create more incentives and ease credit terms for lending to manufacturers** (sic).*

It was therefore no surprise that yesterday's communiqué should have matched the incoherence of the Committee's statement last January.

1) Reviewing recent domestic economic and financial developments, the Committee laments:

*"The Bank had adopted accommodative monetary policy since July 2015 **in the hope of addressing growth concerns in the economy,** effectively freeing up more funds for DMBs by lowering both CRR and MPR."* (emphasis added)

However, the ostensible disappointment at the initiative's failure to produce results is quite disingenuous since t**he break-down of the bank's policy-transmission mechanism had been explicitly flagged** by none other than Deputy Governor Suleiman Barau[2] **during its November session**.

2) Attempting to explain last month's 188 b.p. spike in headline inflation (y/y), the Committee observes:

"Excess liquidity in the banking system was contributing to the current pressure in the foreign exchange market with a strong pass-through to consumer prices."

Unfortunately, this accurate diagnosis directly challenges the claim of exchange-rate stability, made on the preceding page. Left unmentioned is the fact that CBN rationing has so constrained activity on the interbank market that **the parallel market[3] has now emerged as the principal determinant of the exchange rate** and, by extension, the price of imported items.

And so, the Committee restates its predictable *"commitment to maintaining a stable exchange rate"* – a regime that **Standard and Poor's now labels "a fixed arrangement rather than a managed float"**[4].

[1] i.e. MPC member, Dr. Joseph O. Nnana, who was the fraudsters' 'mark'.
[2] See *Personal statement*, at page 49 in MPC Communique No. 104, dated Nov. 22, 2015.
[3] Where the USD currently trades at a 65% premium to the official rate of N197.
[4] Issued only three days before the MPC meeting, *S&P's ratings update* pointedly observed,*'Nigeria's monetary policy has also weakened the country's credit profile, in our view'* – a critique that the Committee chose not to address.

3) The Committee's decision to raise the policy rate by 100 b.p. and the reserve ratio (CRR) by 250 b.p. is nothing less than **a (partial) reversal of the heterodox moves adopted at its November session**[5].

This *volte-face* leaves monetary policy firmly planted in mid-air, a scenario entirely consistent with the sad reality that **increasingly, the relevant decisions are being made in Aso Villa rather than at the CBN**.

[5] The decision also vindicates Dr. Adedoyin Salami's caveat during the November MPC meeting: *"Gross lending rose by N39bn following the net injection of approximately N400bn following reduction of CRR in Sept. [...] Despite the collapse in Money Market rates, banks don't appear to consider lending an attractive alternative deployment for any additional liquidity."* – See *Personal statement* , at p. 75, op. cit.