

Monetary Policy Preview

Caught between the Devil and the Deep Blue Sea

- The Monetary Policy Committee (MPC) is set to meet again amid a global epidemic of the Covid-19 virus which has rocked global markets. At its meeting in January, the MPC hiked the Cash Reserve Requirement by 500 bps to 27.5% in order to curtail the impact of liquidity influx from FI maturity. Now, the CBN is faced with a double whammy of stimulating growth and maintaining FX stability following the impact of Covid-19 on economic activities and global oil prices.
- On FX, the CBN has been embattled with lower oil inflows as well as significant repatriation of foreign flows. Just within the first two weeks in March, the CBN had to intervene to the tune of \$1.8 billion at the IEW. Balance of flows at the IEW is currently printing at a net outflow of \$1.7 billion in March (February: \$1.5 billion). In response to the underlying pressure, the CBN made a couple of adjustments to the exchange rates last week. Firstly, the official interbank rate was adjusted to ₦360/\$ from ₦306/\$. In addition, the following rates were also revised from the prevailing rates of ₦360 – ₦365/\$: IMTOs to Banks – ₦376/\$1, Banks to CBN – ₦377/\$1, CBN to BDCs – ₦378/\$1, BDCs to end-users – Not more than ₦380/\$1.
- Elsewhere, the CBN has also adopted some measures to stimulate growth which includes:
 - i. Extension of principal moratorium on CBN intervention facilities by one year. In addition, the rates on all facilities were reduced from 9% to 5% effective March 1, 2020.
 - ii. Extend its intervention facilities to the pharmaceutical companies, hospital and healthcare practitioners as well as increasing the size of intervention facilities to the agricultural and manufacturing sectors.
 - iii. Creation of a ₦50 billion credit facility for households and SMEs that have been particularly hit by Covid-19.

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- iv. Allow banks to consider temporary and time-limited restructuring of the loan tenor and terms for businesses and household most affected by the outbreak of Covid-19, particularly to the Oil & gas, agriculture and manufacturing sectors.
 - v. Encourage banks to maintain credit to individuals and businesses as well as considering incentives to banks to give out longer tenured facilities.
 - vi. Establishment of a ₦1.1 trillion intervention fund to support critical sectors of the economy.
- Overall, we think the CBN is torn between achieving two conflicting objectives – stimulating growth and maintaining FX stability. For context, while the CBN has embarked on interventions which would increase system liquidity, it is also trying to avoid pressure on the naira via the influx of naira liquidity. Consequently, we expect these two objectives to be major focus at the meeting. In our view, maintaining FX stability would be of utmost importance; however, we do not expect the tactical devaluation by the CBN to keep FPIs given the current global risks and the case of a much-needed single FX rate policy which remains aloof. At best, we expect the CBN to increase OMO rates just to retain some FPIs.
 - Elsewhere, argument for a reduction in the CRR would result into more FX pressure following more naira liquidity. In the same manner, a hike in the CRR would render CBN's interventions counterintuitive. On balance, we think CBN would leave the CRR unchanged while it also stops the debiting of banks with excess liquidity.
 - Given the symbolic nature of the MPR, we think the CBN might opt for a reduction just to give a body language of supporting growth. More importantly, we believe the CBN will opt for the use of more administrative tools and increased interventions. For the former, we can't rule out a restriction of access to FX akin to events in 2015.

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