

**Economic Report | Monetary Policy**
**A static MPC on the horizon**
**Economic Snapshot**
**April 2017 Inflation Data/Indices**

	MoM	YoY	Prev YoY
<b>Headline</b>	1.6%	17.2%	17.3%
<b>Food</b>	2.0%	19.3%	18.4%
<b>All Items Less Farm</b>	1.1%	14.8%	15.4%
<b>Imported food</b>	1.5%	18.1%	18.1%
<b>Energy</b>	1.4%	22.5%	22.5%

**Currency Markets**

	Latest	Daily Chg	YTD
<b>USDNGN</b>	316.5	-0.16%	0.37%
<b>EURNGN</b>	347.1	-0.62%	4.67%
<b>GBPNGN</b>	414.3	0.50%	5.91%
<b>JPYNGN</b>	282.0	0.00%	4.83%

**Monetary Aggregates –April 2017**

	(₦bn)	MoM	YoY
<b>M2</b>	21,713	-1.4%	4.8%
<b>CPS</b>	21,943	-1.5%	13.2%
<b>NGC</b>	5,592	7.5%	42.2%
<b>NFA</b>	7,262	-4.1%	43.2%
<b>NDC</b>	27,535	0.2%	18.1%

**External Position**

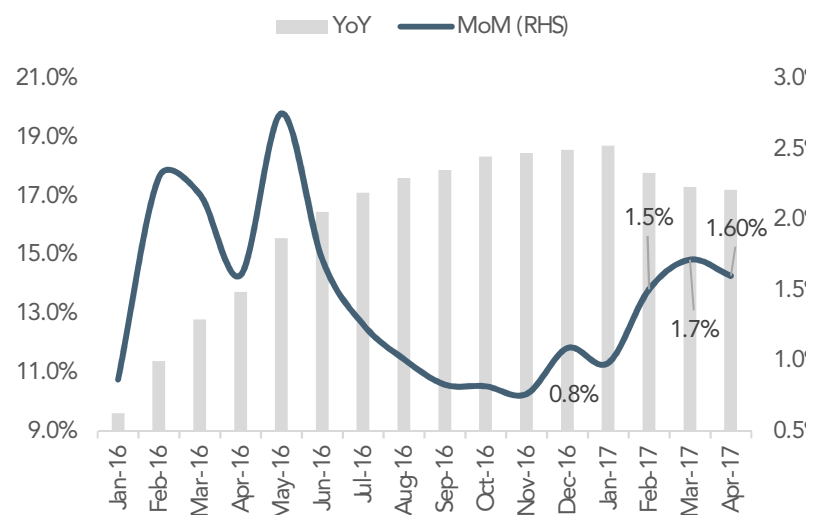
	Latest	QoQ	YoY
<b>Trade Balance (\$'mn)</b>	1583	N/A	N/A
<b>External Reserves (\$'mn)</b>	30,724	5.5%	15.4%
<b>Foreign Debt (\$'mn)</b>	11,406	0.9%	10.4%

**Growth Data – Q4 2016**

	(₦bn)	%of total	YoY
<b>Real GDP</b>	18,292	100%	-1.3%
<b>Agriculture</b>	4,662	25.5%	4.0%
<b>Oil</b>	1,338	7.2%	-12.4%
<b>Services</b>	6,865	37.5%	-1.6%
<b>Wholesale and Trade</b>	3,046	16.7%	-1.4%
<b>Manufacturing</b>	1,757	9.6%	-2.5%

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**Sustained dollar sales to keep naira range-bound**

Today, the Central Bank of Nigeria (CBN) concludes its two-day monetary policy meeting facing a broadly unchanged economic picture on the global and domestic front. On the international scene, monetary policy has remained divergent as slowing economic growth and political worries ensured inert policy changes in the US and Europe whilst declining inflation and tepid growth underpinned monetary easing in some EM countries (Brazil and Russia). On the domestic scene, YoY inflation extended its declining trend for the third consecutive month in April (17.24% YoY) while parallel FX rate continued to trade at a narrow band of between ₦385/\$ and ₦390/\$.

**Figure 1: Trend in Inflation**


Source: NBS, ARM Research

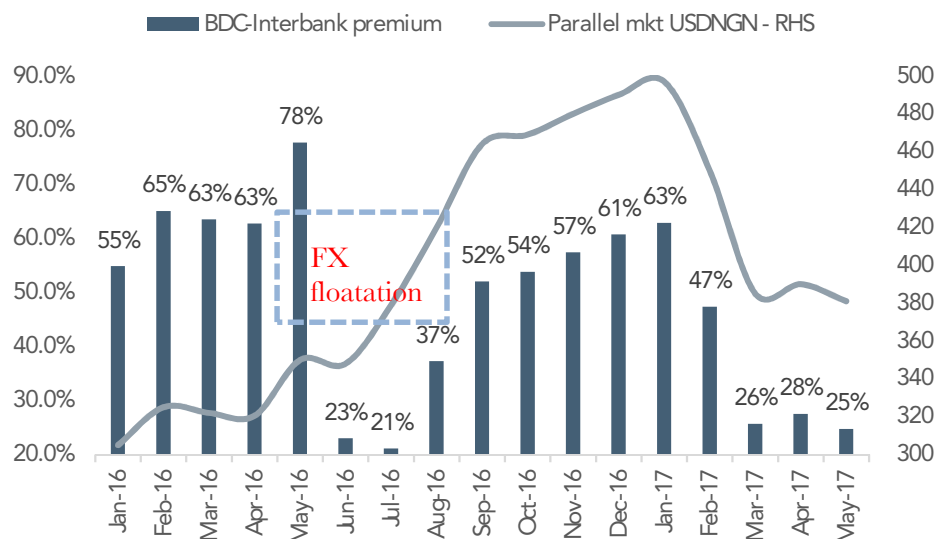
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### *Eyes on inflationary and currency pressures*

In justifying the need for sustained monetary tightening, the MPC at its March meeting noted the upward trajectory in MoM inflation, negative real policy rates as well as sustained pressures in the FX market. Since the last meeting, there's been little changes in these factors. Particularly, despite sustained decline in YoY headline inflation as the base effects continue to dissipate, the MoM inflation reading has remained elevated largely reflecting impact of structural shocks such as higher transaction and transport cost on food prices. Thus, despite the onset of the early harvest season in April which should have applied downward pressure on food prices, MoM inflation rose from February's reading to print at 1.6% in April. Moreover, the decline in YoY inflation reading remained tepid, with the latest headline figure still significantly higher than the policy rate of 14%.

On the currency front, the sub-thirty percent premium between the interbank and parallel market have been sustained for the third consecutive month—first since 2015—largely reflecting improved dollar sales by the apex bank. In addition, CBN's decision to introduce a special FX window for Investors and Exporters whose rates has been largely market driven (between N350/\$ and N400/\$) appear to have been well received by portfolio investors with traders noting significant foreign interest in naira denominated assets. Though, data on capital importation is yet to be updated for the month of April and May, the atypical upsurge in average value traded (+233% MoM) on the NSEASI—akin to the post FX floatation in June 2016—as well as cutback in CBN FX sales to \$682 million so far this month from about \$1.9 billion in April (based on our estimate) appear to lend credence to increased portfolio flows.

**Figure 2: Trend in interbank -parallel market FX premium**



Source: CBN, ABOKI FX, ARM Research

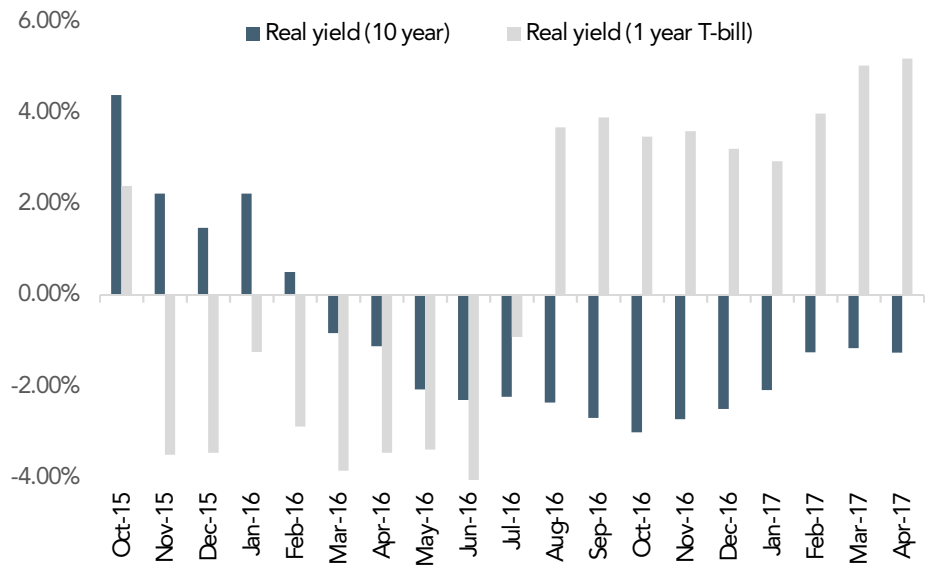
### ***Subsiding output worries to sustain policy inertia***

On the other hand, whilst ongoing monetary tightening continues to push FG’s cost of domestic borrowings higher, it hasn’t prevented the fiscal authorities from implementing its expansionary policy aimed at bolstering economic growth, with annualized spending over the first two months<sup>1</sup> of the year only 4% short of budget. Furthermore, though the country’s real GDP for Q1 17 is expected to be in the red zone, recent data from the PMI reading, improvement in FX supply, resilient agriculture output and higher oil production bodes well for economic outlook over 2017. Already, in April 2017, manufacturing activities expanded for the first time in four months while non-manufacturing PMI contracted at its slowest pace in sixteen months. Hence, given the positive outlook on economic activities, we believe the quest for price stability would remain critical in policy rate decision at this meeting. Since the commencement of sizable FX sales in February 2017, the CBN has kept the banking system relatively illiquid (average overnight rate since February: 33%) with the knock-down effect driving the treasury bill yields higher as it hopes to rid off speculators from the currency market and attract foreign investors with an incentive of positive real return. A reduction in policy rates would likely create a disincentive for portfolio flows which

<sup>1</sup> Only fiscal balance of January and February 2017 has been released

could threaten the stability of the FX market. Thus, given the lingering inflationary pressures as well as the downside risk of a rate cut to CBN's oft mentioned objective of currency stability, we expect the MPC to leave its policy rate unchanged at this meeting.

**Figure 3: Monthly real yields (One year NTB and 10 year FGN Bond)**



Source: FMDQ, ARM Research

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