FUNDAMENTALS

# NIGERIA MPC UPDATE:
## TAKING NO PRISONERS

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# IN BRIEF

- Nigeria's Monetary Policy Committee (MPC) remained steadfast in its hawkish policy stance during the May 2024 meeting, despite acknowledging that the previous policy tightening is beginning to slow the inflation momentum.

- Against our expectation of a "hold" on the policy rate amidst indications of cooling month-on-month inflation, the MPC showed its resolutely hawkish posture with a 150bps hike in the Monetary Policy Rate to 26.25% (Market expectation: 25.75%). The latest decision takes the cumulative policy rate hikes so far in 2024 to 750bps and emphasized the MPC's commitment to restore price stability.

- Evidently, the main drivers of food price pressure are non-monetary and should not ordinarily warrant monetary policy tightening. However, we believe the MPC is focused on taming the potential second-round effects of these non-monetary forces, underpinning its continued hawkish tilt and sustaining the credibility of its commitment to price stability. The persistently strong over-subscription at T-bill auctions also suggests the need for further liquidity tightening.

- Taking stock of the FX market reforms implemented so far, we think the monetary authorities have an eye on strengthening remittances to augment the target rebound in foreign portfolio inflows as key sources of FX market supply. In our view, the unification of the multiple exchange rates and elimination of the premium on parallel market rates resolves the first obstacle to remittance inflows. We also think the licensing of 14 international money transfer operators (IMTOs) is geared towards enhancing competition and eliminating the second obstacle to remittance inflows through official channels as competition trims transaction cost. However, we expect the benefit to be a medium-term outcome rather than a near-term impact. In the near-term, we view foreign portfolio inflows as the more attainable outcome on the back of higher interest rates and market-determined FX rates.

## Resolutely hawkish

Nigeria's Monetary Policy Committee (MPC) remained steadfast in its hawkish policy stance during the May 2024 meeting, despite acknowledging that the previous policy tightening is beginning to slow the inflation momentum. Against our expectation of a "hold" on the policy rate amidst indications of cooling month-on-month inflation, the MPC showed its resolutely hawkish posture with a 150bps hike in the Monetary Policy Rate to 26.25% (Market expectation: 25.75%). The latest decision takes the cumulative policy rate hikes so far in 2024 to 750bps and emphasized the MPC's commitment to restore price stability.

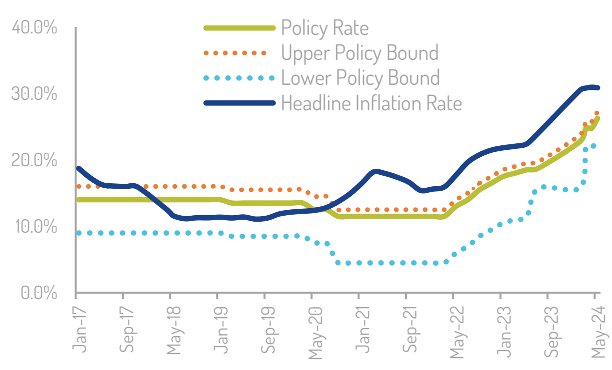
Specifically, the Committee's decision included the following:

- Raise the policy rate by 150bps to 26.25%
- Retain the asymmetric corridor around the policy rate at +100/-300 basis points
- Retain the Cash Reserve Ratio (CRR) of Deposit Money Banks at 45.0%
- Retain the Liquidity Ratio at 30.0%.

**Staying hawkish to consolidate the emerging gains of cooling inflation.** As expected, the MPC alluded to the declines in month-on-month headline, food, and core inflation rates in April 2024 as indications that the recent monetary tightening measures are beginning to yield the desired outcomes.

However, the authorities rightly flagged food inflation as a major conduit of inflationary pressure, which we believe underpinned the MPC's continued hawkishness. The sources of Nigeria's food price pressure mainly include the well-documented issues of insecurity in food production zones, infrastructure-related constraints to distribution network, rising cost of food transport, and exchange rate pass-through to domestic prices. Evidently, these drivers of price pressure are non-monetary and should not ordinarily warrant monetary policy tightening. However, we believe the MPC is focused on taming the potential second-round effects of these non-monetary forces, underpinning its continued hawkish tilt and sustaining the credibility of its commitment to price stability. The persistently strong over-subscription at T-bill auctions also suggests the need for further liquidity tightening.

INFLATION AND POLICY RATE PATH



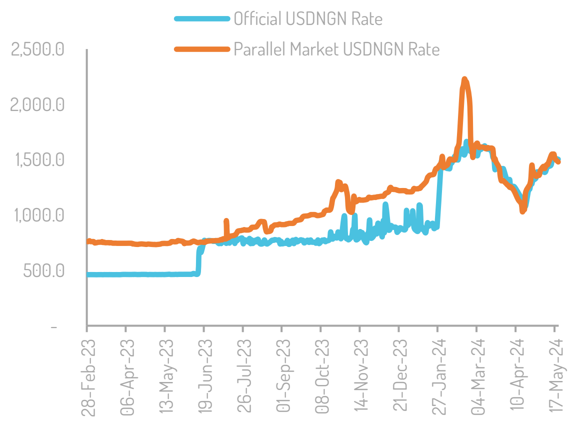

SOURCE: CBN, NBS, IC INSIGHTS.

**Ongoing regulatory measures also aim to improve forex supply via remittance inflows.** At the post-MPC press briefing, the CBN Governor indicated that his interactions with Nigerians in the diaspora revealed two main impediments to remittance inflows via the official channels. These obstacles include the multiple exchange rates and the high cost of transaction on international money transfers.

Taking stock of the FX market reforms implemented so far, we think the monetary authorities have an eye on strengthening remittances to augment the target rebound in foreign portfolio inflows as key sources of FX market supply. In our view, the unification of the multiple exchange rates and elimination of the premium on the parallel market rates resolves the first obstacle to remittance inflows. The MPC expects the recent approval of licenses for 14 international money transfer operators (IMTOs) to deepen competition and lower the cost of transaction in the IMTO space. We think this is geared towards eliminating the second obstacle to remittance inflows through official channels and raises the prospect of improved FX supply as competition trims transaction cost. However, we expect the benefit to be a medium-term outcome rather than a near-term impact. In the near-term, we view foreign portfolio inflows as the more attainable outcome on the back of higher interest rates and market-determined FX rates.

Following a 6.8% m/m decline to USD 32.1bn in mid-April 2024, we observed a modest 1.6% m/m recovery in gross forex reserve to USD 32.6bn as of 16th May 2024. In our view, this reflects the limited FX sale by the Central Bank to Bureau De Change (BDC) operators with the CBN yet to conduct any FX sale so far in May 2024. This has eased the downward pressure on forex reserves, albeit with the resultant tightening in FX supply stoking Naira depreciation pressure so far this month. However, the Central Bank attributes the recent depreciation to seasonal demand, underscoring the effect of a liberalized FX market. In the month ahead, Nigeria's forex reserves could receive further boost from anticipated World Bank approval of USD 2.25bn which we view as FX-supportive.

EXCHANGE RATE DYNAMICS




SOURCE: CBN, IC INSIGHTS

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