**Personal Statement by MPC Members – September 21/22, 2015**

**CBN Communique' No. 103 of the MPC Meeting ... – Sept 22, 2015**

## 1.0 ADELABU, ADEBAYO

Key macroeconomic indicators are suggestive of rising challenges in the various sectors of the economy with the pressure emanating from both the global and domestic environments. The recovery in the global economy has remained largely uneven with the balance of risks tilted to the downside. Among the industrial nations, only the US and UK appear to be recording fairly impressive growth while the vast majority, particularly the Euro zone, is grappling with one challenge or the other. The lingering challenges of deflation and turbulent financial market in the Euro zone have now been compounded with the issue of illegal immigrants in Germany. As a result, the earlier growth projection of 3.5 per cent for 2015 has been revised downward to 3.3 per cent. The condition is not anything better in the emerging economies with most of them showing downward trend. China, one of the biggest emerging economies is now on a lower growth trajectory of around 7.5 per cent relative to the average of double digit in the first decade of the century. The slowdown in global economic activities coupled with the rising global supply of crude oil has considerably moderated the prices of crude oil with far reaching implications on the domestic economy.

The domestic economy is further challenged by elevated headline inflation, which rose to 9.2 per cent in July 2015 and remained flat in August, largely due to acceleration in food inflation. More worrisome is the development in real output as the GDP growth of 2.35 per cent in the second quarter is not only below the 5-year average, but also represents a second consecutive slowdown. The financial markets have continued to witness considerable level of volatility particularly in the month of August with an average interbank rate of about 31 per cent. The commencement of full implementation of the TSA could have contributed to the spikes but it is most welcome that the initial spikes are dying off.

Although equities and fixed income securities have shown partial recovery following the successful conduct of the elections, they have underperformed relative to emerging markets peers, suggesting some level of reservation by investors. The recent exclusion of government bonds from the JP-Morgan EM index could have also contributed but the effects appears to be waning. The exchange rate market is less volatile at the interbank segment but the burden was borne by the external reserves, which declined by 4.2 per cent between July and August, indicating persistence of demand pressure.

Against these multi dimensional challenges, monetary policy needs to take a cautious approach to avert the danger of time inconsistency. With respect to the headline inflation, the medium term upside risks include the likelihood of commencement of hike in interest rate by the Federal Reserve with the attendant strengthening of dollar which could rapidly impact on domestic price level from exchange rate pass through effect. As valid as this argument may sound, there is a countervailing factor in the sense that the base effect has contributed significantly to the current uptick in headline inflation given that the month-on-month metric showed moderation. It should be therefore, expected that an improvement would be recorded as the base effect dies off by end-December.

With respect to the slowdown in growth, as I have argued in my previous statements, the underlying causes are largely structural in nature and this seems to have been corroborated by the rising contribution of food inflation to the overall headline inflation; a clear indicator of food supply deficit. The structural bottlenecks have been largely caused by the activities of insurgents and hiccups around production and distribution system. It is remarkable that considerable success is being achieved by the Federal Government in the fight against the insurgency and this should translate to improvement in output level soonest. Besides, complimentary factors that could enhance the ease of business environment should not be discounted in order to promote foreign direct investment.

With regard to the financial markets particularly the pressure on the exchange rate, the key drivers include the adverse shock to the terms of trade in the form of slump in the price of crude oil. The phenomenon may not be reversed soonest owing to supply glut in the global oil market. It is envisaged that that it would take several years of ongoing retrenchment of capital expenditure in the oil sector to rein in global supply. Besides, if the downturn in financial markets in Europe and China snowballs into wider real financial crisis, commodities prices including oil could overshoot downside forecast. Thus, prudent demand management measures already in place, particularly the exclusion of certain items from the interbank foreign exchange market, need to be pursued to a logical conclusion. Besides, the ongoing turn around in the domestic refineries would go a long way to reduce demand pressure in the foreign exchange market. Thus, I would advocate for fast tracking of this process.

On the banking system efficiency in general, I advocated in my last statement for remuneration of part of the sterilized fund as a palliative measure towards reducing the cost of financial intermediation to the banks. Evolving developments since that time are suggestive of stronger liquidity enhancing measures. My position derives strong support from the fact that current macroeconomic conditions pose threat to the banking sector from both the asset and liabilities sides. From the asset side, apart from the provisioning that could emanate from exposure to oil and gas sector, current data shows that the stock market fell by about 11 per cent by end-August. This would adversely impact on the balance sheet of firms because it implies a reduction in the net worth of firms and companies quoted on the stock exchange by about 11 per cent. In view of the existence of strong information asymmetry in Nigeria's credit markets, a lower net worth leads to a more severe adverse selection and moral hazard in lending to those firms. In other words, lower net worth implies a lower collateral for the loans extended to those firms, therefore banks would be constrained to reduce their exposure to these firms with dire consequence for future growth and employment. This issue needs to be brought to the front burner in the light of negative growth in the manufacturing sector in the last two quarters.

The liability side on the other hand, would suffer initial setback with the full implementation of the Treasury Single Account as the latitude for deposit mobilization is reduced, ultimately affecting liquidity and lending. In sum, evolving macroeconomic conditions would reduce the scope for financial intermediation. It needs to be underscored that economic contraction is accentuated in an environment of financial instability and the primary approach for a central bank to avert financial instability is by ensuring liquidity in the financial sector in order to prevent initial crisis from spinning out of control. This has been aptly demonstrated by notable central banks on a number of occasions. For example, the US Federal Reserve in the fall of 1998 had to reduce the Federal Funds rate by 75 basis points to avert the spillover of Russia financial crisis on the US financial system. Against this perspective, I am of the view that the existing cash reserve requirements should be reduced in order to enhance market liquidity and inevitably enhance financial intermediation.

Based on the foregoing, I would like to propose a reduction in the existing CRR by 600 basis points to 25 per cent while the MPR and the LR are retained at the subsisting 13 and 30 per cent, respectively. The symmetric corridor of 200 basis points on the MPR should equally be maintained.

## 2.0 ALADE, SARAH O.

A number of challenging events have affected the Nigerian economy since the last MPC meeting in July. These include the announcement by JP Morgan that the country will be delisted from the emerging market bond index at the end of September and the total adoption of Treasury Single Account (TSA) which moved Federal Government Funds from the banking system into government accounts at the Central Bank. Despite these events, the Nigeria economy has shown some level of resilience and has weathered the storm remarkably well. In the domestic environment, Nigeria like other commodity exporters is experiencing tighter external financial conditions and an uptick in headline inflation. In addition, lower oil prices is helping to fuel turbulence in the foreign exchange market and a bearish situation in the stock market as investors divest their portfolio away from the Nigerian market. Based on the above, I support a hold on Monetary Policy Rate (MPR), and a reduction in CRR to 25 percent to release liquidity to the banking system and to allow banks to adjust to the adoption of TSA in the short run.

***The growing cloud over global growth has prompted the Federal Reserve to maintain benchmark interest rate at near-zero percent at its September 17th Meeting***. Coming out of its Federal Open Market Committee (FOMC) Meeting, Fed Chairman stated that "recent global economic and financial developments may restrain economic activity somewhat and are likely to put further downward pressure on inflation in the near term" for the US economy, thus a rate hike is further delayed till end of 2015 or early 2016. Growth in emerging market and developing economies is projected to be lower as low commodity prices and tighter financial conditions pose increasing risk to growth in the region. Concern about global economic slowdown, low inflation in the US and volatile stock markets informed the Fed decision to keep rate steady. Heightened concerns about growth in China and other emerging market economies have led to notable volatility in financial markets. Oil exporting countries have had to revise their growth projection downwards. In view of these developments, monetary policy is expected to remain responsive to the emerging issues these developments pose for the Nigerian economy.

***Headline inflation increased to 9.3 percent in August compared to 9.2 percent recorded in July 2015.*** Headline inflation increased to 9.3 percent in August from 9.2 percent recorded in July. This is the third consecutive month that headline inflation has surpassed the up limit of the Central Bank inflation target of 9 percent set since 2013. Both core and food inflation rose in the review period. Core inflation rose to 9 percent from 8.8 per cent in July, while food inflation increased to 10.1 per cent from 10 per cent in the previous month. The uptick in year-to-date inflation rates can be traced to the late start of the raining season, which has delayed harvest and insurgent activities that limited farming activities in the North Eastern part of the country. While the rains have commenced, some of the time lost may not be regained, thus medium term outlook for inflation may remain elevated to the end of the year. Based on this, monetary policy should give consideration to the feedback effect of the food supply seasonality on the economy.

***Medium term growth projections remained subdued with further downside risks***. Economic growth continues on the downward trend, as real GDP grew by 2.35 percent during the second quarter of 2015 compared to 3.96 percent recorded in the first quarter. This was lower by 1.61percentage points from growth recorded in the preceding quarter and also lower by 4.19 percent points from growth recorded in the corresponding quarter of 2014. Non-oil growth was subdued, growing by 3.5 percentage points, lower than 5.6 percent in the first quarter. The subdued growth is attributable to lower oil price which resulted in lower government revenue, the feedback effect of fuel disruptions as a result of the stand-off between oil marketers and government and foreign exchange scarcity. The drop in oil price reduced export earnings by 40 percent year-on-year, putting pressure on the foreign exchange market and reserve level. Despite these challenges, the Nigeria economy remains resilient but policy actions will be needed to secure the gains made. In the coming months, as government economic policy is articulated, and a conducive environment is created to attract foreign and domestic investors, the downside risk to growth could be reversed.

***Against this background,*** care must be taken to navigate the precarious global environment and its impact on Nigeria. Given the divergent monetary policies on the global scene, rising inflation, declining growth and lack of fiscal buffers in the domestic environment, a hold on policy rate is needed in the short term. In addition, the adoption of TSA would have impact on liquidity in the banking sector and an increase in policy rate could be detrimental to the system at this time. Also at a time that JP Morgan is delisting the country from the Emerging Market Bond Index, it is important that the banking system remain liquid. Base on this, I vote for a hold on policy rate, and a reduction of Cash Reserve Requirements (CRR) to 25 percent.

### 3.0 BALAMI, DAHIRU HASSAN

Global growth remained mixed after the last MPC meeting. This is particularly true with Nigeria's major trading partners' economies including the Euro zone (i.e. countries like France, Germany, UK, Italy and Spain etc) and others such as the U.S.A, Canada, India, China, Brazil, Argentina and Japan. Global trade level remained weak with the value of World trade down by one per cent (1%) except in Africa and the Middle East. Other happenings that have direct bearing on the Nigerian economy include the following:

(i) Weakening industrial production in the Euro zone, with the exception of construction, declined by at least 4%;

(ii) Current decline in World net export trade with the exception of Africa and the Middle-east;

(iii) Monetary tightening in the U.S and the Strengthening of the U.S Dollar;

(iv) Falling oil price at the international market and

(v) The uncertainty with Greece economy and the expected future negotiations.

The implication of the following on the Nigerian Economy is the slow domestic economic growth in the second and third quarter of 2015. Although domestic demand from the major trading partners is high as demonstrated by Purchase Managers Index (PMI), it will take some time to impact on the Nigerian economy positively. In my opinion, the CBN, FMF and DMO have taken the right decision by protecting access to foreign exchange.

The level of growth at the domestic level has been on the decline while inflation is on the increase. This is reflected in the decline in the level of asset, credit and increasing level of non-performing loans. The policy decision is whether to promote growth or tame inflation. In my opinion the better option is to promote growth.

The foreign exchange market has been relatively stable particularly in interbank rate which has fluctuated between N196 -197. However this is possible due to earlier policies of the CBN.

**Concerns about the Nigerian economy**

(I). The terrorism and insurgency in the Northeast region, Niger Delta and Oil theft are still on-going, affecting the level of growth in the agricultural sector, trade and commerce, etc.

(ii). The growing level of youth unemployment in the economy especially in the North East and the problem of the IDPs and the cost of planned resettlement and reconstruction. This will put much pressure on the resources of the government at all levels

(iii).The non-execution of many capital projects in Nigeria in 2015, implies series of future problems for the economy.

(iv). Structural deficiency between demand and supply constraints on the foreign exchange market.

(v). The poor performance of the capital market due to losses in September 2015 in which some of the major DMBs stocks were hard hit.

(vi). The declining level of foreign exchange as a result of volatility in the crude oil price and quantity exported has greatly affected Nigeria's external reserve.

In my judgment, to promote inclusive growth, job creation and development in the economy, there is need for the rehabilitation of the infrastructure in the North-east region in particular and Nigeria in general; and further liberalize trade and commerce by executing various development projects and opening up the routes that were closed as a result of the activities of the terrorists. Various initiatives and assistance for development of the devastated areas should be consolidated for effective planning and execution. The costs of borrowing need to be lowered to encourage entrepreneurs to take advantage of the investment opportunities in the North particularly with the ongoing improvement of the security situation. The operation of the TSA when fully implemented will have positive implication for the economy.

The ability of the policy makers to stabilize the exchange rate at the official window for the past seven months is commendable and should be encouraged.

I therefore vote to:

(i) Reduce the Cash Reserve Ratio Requirements from 31 to 25 %. This will raise the level of liquidity in the economy. It will also prepare the DMBs for October 2015 as well as complete delisting of the FGN Bonds from the FGB-EM by JP Morgan.

(ii) Retain the MPR at 13%

(iii) Maintain symmetric corridor of +2/-2%.

In my mind the monetary and fiscal space should continue to monitor developments in the economy and take necessary policies that will protect the economy and the Nigerian interest.

## 4.0 BARAU, SULEIMAN

**Background**

My assessment of current macroeconomic conditions reveals rising imbalances in virtually all sectors of the economy. In the external sector, sustained negative term of trade shock via the slump in oil price is driving the balance of payment to a disequilibrium level, the first time in over ten years. Furthermore, imbalances continued in the foreign exchange market with demand pressure outstripping supply, culminating in negative accretion to external reserves between July and early September.

Imbalances in the domestic environment include dwindling fiscal revenue relative to expenditure, suggesting imminent twin deficits of fiscal and current account deficits. Imbalances also exist in the real sector as both public and private domestic demands are partially suppressed on the backlash of dwindling public sector revenue and the attendant non-payment of salaries at some levels of government thus, constraining output growth, among others. Estimated GDP for the second quarter was 2.95 per cent, the lowest in the last five years, while inflation for August was 9.2 per cent.

The imbalance in the banking sector is becoming clearly discernible with deterioration in asset quality due to the effect of falling oil price on exposure to oil and gas sector, which constitutes a reasonable component of banking sector assets.

On the flip side however, efforts at eliminating wastes by the new administration and progress recorded in the fight against insurgency have bolstered confidence in the economy and this is expected to reverse negative sentiments from foreign investors but it would take some time and complimentary actions for the confidence to impact key macroeconomic variables.

It is obvious that monetary policy tools may not be sufficient to simultaneously address all of these imbalances, thus requiring strengthening the synergy between the fiscal and monetary authorities. I am therefore of the view that the best approach for the monetary authority is to focus on maintaining stability in the macroeconomic environment in order to strengthen the confidence emanating from the new political dispensation. Given the importance of banking system stability to monetary policy transmission mechanism and by extension overall macroeconomic stability, I would advocate for measures that could reduce part of the strain on the banking system. Consequently, I would like to propose a reduction of the consolidated CRR by 600 basis points to 25 per cent with a view to enhancing intermediation process. I would, however like to maintain the MPR and LR at 13 and 30 per cent, respectively.

**Issues and Pressure Points**

Developments in both the external and domestic macroeconomic environments continued to reveal intensification of risks.

**External Environment:** Apart from the US and UK, most global economies have been facing challenges as a result of which global recovery remains muted and unevenly distributed. Earlier global growth projection of 3.5 per cent for 2015 has been revised downward in the second half of the year by 0.2 percentage point but more fundamentally, the balance of risks tilted towards the downside and heavily skewed against emerging market economies (EMEs). In the advanced countries, the unresolved problems of deflation in the Euro zone and the challenge of Greece debt crisis have further been complicated by the challenge of illegal immigrants in Europe.

In the emerging economies, the Chinese economy, one of the biggest emerging market economies, is now facing slowdown on the heel of shifts in its growth model from exports to consumption while the stock market has just crashed by about 30 per cent. A significant slowdown in China would affect Nigeria in at least two ways: export to China may suffer severe setback with negative consequence for our current account while the challenge in the financial market could make investors flee to the US, leading to further appreciation of US dollar against emerging economies currencies, including Nigeria.

Another key challenge from the global economy is the lingering slump in crude oil price. The dynamics of the oil market is indicative that crude oil price may well anchor below US$55/barrel over the next two years. The August 2015 data revealed that Brent crude traded as low as US$42/barrel on the backlash of massive sell off. With the re-admittance of Iran to the oil market coupled with rising investment in exploration in many parts of the globe such as North America, the Middle East and Africa, global output would continue to exceed demand in the near to medium terms. This, invariably, would continue to pose challenge to the current account as well as fiscal revenue.

In addition, the declining capital inflow and rising outflows have not abated. The recent exclusion of the country from the JP-Morgan Index may be seen in certain quarters as an issue but I do not see much challenge from it. My take is reinforced by the latest data on bond yield, which showed that the initial spike, after the announcement of the exclusion, has died off. The real issue, however, is the much anticipated hike in interest rate by the Federal Reserve. Latest information suggests that the delay in announcing the hike at the September's meeting was due to the need for clarity on non-farm statistics as other indicators supported the announcement. Thus, it should be reasonably expected that this would come in the early period of next year, at the latest. This has at least three implications on the economy. First capital outflow would accelerate. Second, dollar would strengthen against most currencies with implication of higher inflation through exchange rate pass through. Thirdly, banking system stability may be threatened as dollarization may increase with implication of reduction in naira denominated deposit liability.

**Domestic Environment:**

Key macroeconomic indicators showed signs of further weakness up to the early part of the third quarter. The GDP recorded a slow down for the second consecutive quarter, growing by mere 2.35 per cent in the second quarter, down from 3.96 and 6.54 per cent in the previous and corresponding quarters, respectively. More worrisome is the development in the industrial sector which recorded negative growth at -1.11 and -1.02 per cent in Q2 and Q1 of 2015, respectively. This is a clear signal that unemployment may increase in no distant time. Meanwhile, the latest data from the Bureau of Statistics revealed that underemployment increased to 17.9 per cent in Q4, 2014 from 15.4 per cent in Q3, 2014 and 14.8% in 2013. Despite the benign global inflation environment, domestic headline inflation remained flat at 9.2 per cent in August, having been trending upward for seven consecutive months. The present level of inflation is the threshold of the target set by the Bank as possibility of further slippage remains a course for concern.

Analysis of fiscal profile shows serious revenue shortfall at the end of June. Cumulative fiscal deficit at the end of June was about N676 billion, annualizing to about N1.36 trillion against the projection of N755 billion in the 2015 budget. This, invariably, has put pressure on monetary sector with credit to Government growing by over 150 per cent at end-July 2015. As expected under this circumstance, private sector has been crowded out with private sector credit growing by mere 3.29 per cent at end-July 2015. This portends adverse implication for future investment and ultimately growth and employment.

The financial markets have shown relative degree of stability but not without some strains. The interbank rate exhibited considerable spikes in the month of August with an average of about 31 per cent but data in September suggests that some calmness has returned to the market. The strain in August must have been due to the initial market reaction to the implementation of Treasury Single Account (TSA) although the implementation of the TSA would reduce the level of liquidity in the market considerably, going forward.

Developments in the foreign exchange markets also suggest an underlying rising pressure. The interbank rate has been fairly stable but the pressure was borne by the external reserves, which declined by 4.62 per cent between July and August 2015. Furthermore, the premium between the interbank and the BDC rate remained perpetually elevated at about 24 per cent, providing opportunities for arbitrage.

**Considerations**

The key considerations for my decision are as follows:

i. **Need to Manage the Inflationary Pressure:** A critical pillar of monetary policy is the capacity to anchor expectation of economic agents. With headline inflation of 9.2 per cent in August, the single digit threshold of the Bank is seriously threatened. The direction of inflation over the medium term is a little bit dicey in view of equally strong upside and downside risks. The upside risks include the seasonality factor particularly the end of the year festivities. The second one is the likely increase in aggregate demand resulting from the recent bail out to states while the third risk actor is the likely appreciation of dollar due to increase in interest rate by the Federal Reserve. Although the drop in oil price is providing tailwinds for global inflation, the much anticipated hike in interest rate by the Federal Reserve with the attendant strengthening of dollar would filter into domestic price level through exchange pass through. The foregoing notwithstanding, there are some other countervailing factors that could be at play. First, the rise in headline inflation since January was on year-on-year basis as the month-on-month showed moderation, suggesting base effect. Secondly, a large portion of output gap was due to the activities of the insurgents in certain parts of the country, thus with the significant progress in restoration of peace in these regions, economic activities would likely resume in full swing. In view of this apparent balance of risks, it may be in order to leave the policy rate unchanged particularly when cognizance is taken of the deteriorating performance of the industrial sector.

ii. **Need to Avert Disruptive Movement in the Exchange Rate:** The interbank exchange rate has been relatively flat in the last couple of months but at the expense of the external reserves while the premium between the interbank and the BDC rates at about 24 per cent is clearly above the tolerance limit. It needs to be underscored that the ripple effects of the unsettled financial markets in Europe and China would not be limited to only financial assets, commodities markets particularly oil and other primary exports of developing countries would be affected. Consequently, additional pressure may be exerted on external reserves. Reflecting likely crystallization of this risk, all emerging countries currencies have been under pressure in recent times. In the last one month, notable emerging countries currencies such as Chinese Yuan, Vietnam Dong, and Kazakhstan Tenge have been devalued. In the present circumstances where the supply side of the foreign exchange market is facing intensive shock, it may be necessary to strengthen demand management measures. Nonetheless, the moderating impact of the TSA on the excess liquidity of the banking system would likely reduce excessive demand pressure in the market. Thus, additional measures may not be necessary for now.

iii. **Need to improve Financial Intermediation by the Banking Sector:** The balance sheet of the banking industry is threatened from both the assets and liabilities sides. The interbank rate could have normalized after the initial shock from the implementation of the TSA, nevertheless sustained compliance with the TSA concept would reduce the scope for deposit mobilization and ultimately affect intermediation process. When this is combined with shocks to the asset side such as delinquency on exposure to oil and gas sector, classification of consumer loans to public servants due to non-payment of salaries, and restructuring of states and local governments loans, the stability of the banking sector may be threatened. It may be therefore expedient to free some of the sterilized funds under the subsisting CRR with a view to improving financial intermediation. This is more important when the emerging ugly trend of negative growth in the manufacturing sector is taken into consideration.

iv. **Need to Avoid Time Inconsistency in Policy:** It is intuitive appealing to ease policy stance on the backlash of slowdown in GDP. However, as I have argued in my previous statements, most of the drivers of the slowdown are traceable to structural bottlenecks within the economy rather than monetary factors alone. Besides, easing of interest rate in the face of strong pressure from the external sector could only add to the imbalances which would discourage investments and thereby accelerate recession.

**Decisions**

In the light of the foregoing, I would like to propose a reduction in the consolidated CRR by 600 basis points to 25 per cent while the MPR and LR are maintained at the subsisting rate of 13 and 30 per cent, respectively. In addition, the symmetry corridor of 200 basis points around MPR should be retained.

## 5.0 GARBA, ABDUL-GANIYU

### Context of Decision

The greatest danger to economies (large, emerging and small) in the post-2007 global economy is the risks posed by a lack of depth, scope, memory or foresight in the analysis that supports policy decisions. As I wrote in my personal statement of March 2014 MPC: ''these are challenging times for all monetary authorities all over the world primarily because the world is in unfamiliar territories in which unconventional monetary policy instruments have been deployed in the post-2007 global financial crisis by the most powerful Central Banks. In the process, they have created financial and economic challenges of unprecedented depths, scope and length." A key consequence is the emergence ***two twin traps*** - a low interest rate and quantitative easing trap (large economies) and high interest rate and tightening trap (small and ''emerging" economies). In addition, the balance of power in the policy game has shifted in favour of the ''market" such that if policy makers fail to understand the new policy environment, they would be prone to short-sighted and catastrophic policy choices. To safeguard the medium and long term health of economies, policy makers must avoid short memories, lack of depth, scope and foresight in the very difficult policy environment of the new epoch.

I first warned about the dangers of the two related interest rate traps in my personal statement of November 2013 MPC when I wrote:

''Available evidence leads me to conclude that the major economies (United States, United Kingdom and the Euro Zone) are sinking into a low interest rate trap. The decision of the European Central Bank (ECB) to cut its Monetary Policy Rate by 0.25% exemplified my point. The President of the ECB justified the rate cut on the ground that the annual inflation rate fell below 1% - (the target rate is 2%). The forward guidance was to the effect that as long as there was fear of deflation, monetary authorities will cut rate and sustain the policy of monetary accommodation. The forward guidance traps the ECB and similar Central Banks to (persistent) low interest rates and quantitative easing (QE) trap''. The evidence then showed ''that several episodes of monetary accommodation since 2007 (had) failed to stimulate aggregate demand to the degree of the QEs.'' Analysis of the transmission mechanisms of monetary policy in large, emerging and small economies convinced me that ''much of the monetary accommodation (was) "dammed" in the financial markets causing (i) inverted intermediations between central banks and financial market players; (ii) distortions in asset and commodity pricing and allocation and (iii) concentration in wealth.'' It was clear to me that in the case of ''Nigeria, the low interest rate trap is a danger to financial stability (because) the high interest rates and stable currency in Nigeria (had) been attracting portfolio flows into equity and money market instruments well beyond their optimum levels.'' The flip side was the attractiveness of borrowing by DMBs and Nigerian firms in foreign currency raising the risks of currency mismatch when the exchange rate comes under pressure.

The analysis led me to warn that ''such flows in a globalized asset price bubble environment (can mislead) many players (to) become complacent on the false expectations that the flows will continue (and that) Nigeria has gone through painful "bubble asset" withdrawal syndromes before . . . (and) it will be costly to go through a full scale bubble asset withdrawal syndrome again. The greatest danger to policy effectiveness, financial and economic stability (was) the high likelihood that global low interest rate trap and, domestic fiscal dominance (were) leading monetary policy into a high interest rate regime. It was clear to me then in November 2013 that it ''was of the outmost importance that Nigeria avoids a high interest rate trap and its twining with the low interest rate trap.''

In the personal statement of January 2014, I re-emphasized my concerns about the two interest rate traps and their structural hysteresis (long term consequences). By digging themselves into the low interest rate and quantitative easing trap I was and still am convinced that the large economies, have weakened the transmission mechanisms of policies (monetary and fiscal) globally, distorted the financial-real economy relationships and caused financial markets to malfunction in the allocation and pricing of financial assets. The episodic volatilities and the large amplitude observed in August 2015 in global financial and commodity markets are some of the consequences of the uncertainties and risks generated by the low interest rate trap. It was not a surprise that the US Fed, Bank of England, the European Bank, Bank of Japan are unable to raise rates nor are they able to stimulate upward movements in aggregate demand and prices. The recovery of employment in the US has proceeded without growth in income and with uncertainties in the global economy; forward looking economic agents are unlikely to spend without concern about future risks. The global concentration in wealth clearly, weakens growth in aggregate demand hence, the possibility of inflation.

Emerging and some small economies including Nigeria imprudently walked themselves into a high interest rate trap in their scramble to attract portfolio flows despite the short term trade trade-offs (job, efficiency and growth) and medium to long term trade-offs (jobs, efficiency, growth and macroeconomic and financial market instability). The danger was most acute for economies committed to exchange rate stability and free capital flows because the monetary policy was easily trapped into a high interest rate regime: the fear being that easing will trigger devaluation pressures on the exchange rate as Nigeria is currently experiencing. Those who underplay the importance of a loss of capacity for independent monetary policy that most central banks (large, emerging and small) have walked themselves into cannot provide the light for restoring the transmission mechanism of monetary policy, the stability of markets (financial, labour and product) or the stability of the macro-economy.

It was clear to me that a stable exchange rate and price regime could very easily unravel if a forward looking economic management strategy comprising of a creative mix of complementary macroeconomic policy (monetary and fiscal), macro-prudential policy and micro-prudential were not developed in time and effectively implemented. I warned that it was ''in the best interests of Nigeria that its policy makers are not caught unprepared.'' This was partly why I voted for the discriminatory CRR on public deposit in July 2013 and January 2014 (to impose fiscal prudence and shut down the game of corporate welfare and unnecessary accumulation of public debt when government had deposits of about three trillion Naira in Deposit Money Banks). This was why I also consistently expressed my preference for ''a forward looking fiscal policy regime . . . (anchored in a commitment to the fiscal rules in the Fiscal Responsibility Act of 2007 and ''a strategic and forward looking management of oil and gas resources'' to build forex reserves required to support a stable currency.

Had fiscal policy been forward looking, public savings would have been built up and the fiscal buffers would have minimized the effects of the shocks (commodity price collapse, bubble corrections and reverse flows) whose likelihood of occurrence were obviously very high. The path of Nigerian money, capital and forex markets particularly since October 2014 justify the concerns raised in my personal statement of November 2013 about the twin traps and the vulnerabilities they pose to large, small and emerging economies.

In my personal statement after the March 2014 MPC, I had expressed concerns that ''many global players do not (1) see the linkages and the medium term strategic implications and/or (2) have no interest in the ***global commonwealth.*** For such short-sighted players, exploiting the asymmetries at the nexus points is fair game (rational) regardless of the resulting turbulence and the social, political and economic consequences. Yet, unless many Central banks and market players see, understand and submit to the good of the global commonwealth, the turbulence in the global economy and its disturbing consequences will persist for a very long time to come. A beggar thy neighbour policy environment is ***globally inferior*** to a mutually beneficial cooperative environment." I had argued for a global cooperative process to solve the problems of the twin traps because I was convinced that the ''two traps demand (1) a forward looking monetary policy ***process*** within a broader and longer space-time horizon and (2) greater mutually beneficial policy coordination between monetary and fiscal authorities and between Central Banks regionally and globally. Otherwise, ***exiting the abnormalities of the last few years will be painful for most and unsettling for all."***

I pointed to the fact that ''the various options for disposing the toxic assets (mortgage backed securities) that the US Fed and most Central Banks had accumulated on their balance sheet . . . (were) fraught with dangers for monetary policy, for global financial markets (asset prices, interest rates and yields), for the housing markets and for growth and employment." I was convinced that fiscal-monetary policy coordination in Nigeria would have helped to build buffers and made both policies more effective and more compatible to medium and long terms economic goals of Nigeria.

I have provided this rather detailed chronology of my personal statements to underscore the real challenge of macroeconomic management in the post-2008 world and the risks of policy making within a narrow scope and a short time horizon. The greatest danger which most leading policy makers chose to underplay is deeper, long-termed and deeply structural: the challenge of traps. Listening to and watching Fed Chair Janet Yellen's press conference after the September 17 2015 Federal Open Market Committee (FOMC) meeting I was struck by an unwillingness to confront the new post-2008 global economic realities. As much as Fed Chair Janet Yellen tried to downplay the threat of the Fed being in a zero interest rate trap, she did not rule it out but had no plan B. She was asked ''Are you worried that, given the global interconnectedness, the low inflation globally, all of the other concerns that you just spoke about, that you may never escape from this zero lower bound situation?" Fed Chair Janet Yellen answered ''So I would be very—I would be very surprised if that's the case. . . Can I completely rule it out? I can't completely rule it out." Clearly, there is no Fed strategy to dig itself out of such a trap and the associated costs. Japan which entered into such a trap in the aftermath of its asset market bubbles of the late 1980s is yet to exit the deflation trap. Now the major economies had joined it.

To ignore the current realities of the global economy and its implications for economic and financial outlook is to increase the chances of dangerous policy errors. As I pointed out in my personal statement after the July 2015 MPC, the real policy choice is not between tightening or easing. It is far ''more fundamental. It is about institutions, incentives, strategy, coordination and forward looking. At the heart is the primacy of mechanism design and about leveraging on the new government's positive signals about fiscal prudence, consolidation of NNPC Accounts in the Central Bank and possibility of re-starting production in the refineries to develop a macroeconomic management strategic framework for Nigeria." This remains my position at this MPC meeting.

**Decision**

I vote to hold.

However, my vote to hold is not a vote to do nothing. Rather, it is a vote to harness and direct all available intellectual and political resources to engage the fiscal authorities to develop a macroeconomic management strategic framework for Nigeria urgently to meet the ***real*** challenges of macroeconomic management in this new epoch.

The CBN Act makes it clear that the primary mandate of the CBN is price stability and its secondary mandate is to support the policies of the government. Neither mandate could be successfully achieved without a dynamic and efficient and effective coordination of fiscal and monetary policy and without a comprehensive and consistent strategic framework for monetary policy, macro-prudential policy, micro-prudential policy and development finance policy. Developing the frameworks for me, are the real and urgent challenges.

It is true that the macroeconomic and financial market outlooks are precarious for Nigeria and for most small and emerging economies and indeed for most of the global economic zones besides the US. However, doing something is not necessarily prudent. Similarly, a reactive one issue driven monetary policy in the current policy environment is most likely short sighted and prone to costly errors. For instance, had the discriminatory CRR prevailed until the policy of Treasury Single Account (TSA) came into force under the new regime, there would have been no need to raise private sector CRR to 31% at the May 2015 MPC. The process of adjusting to the TSA after September 15 deadline would have generated less ''noise'' since 75% would already have been in the CBN and with CRR at 20% the effect of TSA on system liquidity would have been marginal if at all. In any case, there was sufficient forward guidance between July 2013 when the CRR on public deposit was increased to 50% about the need for Deposit Money Banks to gradually change their business model from one that depended on profits from lending public deposits to government to one that depends on intermediation between borrowers and savers for their profits. Clearly, their preference for ''financial subsidy" was rational but short sighted and very costly for fiscal and monetary operations. In addition, the ''strategic noise" about illiquidity is not supported by the data on the average Liquidity Ratio which was at least 10% above the required rate.

The expectation that a reduction in CRR will lower short term rates is not rooted in sound analysis or evidence. The strongest argument for lowering CRR is the profit argument. Yet, there is the unresolved ***profit puzzle:*** rising profits of DMBs while growth in credit, assets and deposits are slowing and inefficiencies are rising (interest rate spreads, operating costs and forex arbitrage opportunities). In any case, liquidity management implies that OMO could be used to mop-up excesses liquidity or to inject liquidity when necessary. The size of the projected injections through reduction in CRR to 25% increases in the risks of exchange rate pressures given the asset structure of the DMBs in the last few years. It will be imprudent to begin to raise CRR in subsequent MPC meetings when the liquidity injected begins to exert pressures on the forex market. This is more so, since OMO could be used inject liquidity and reduce the cost of mopping up later. Given the risks to the forex market and to financial system stability of further pressures on the Naira, I could not vote for a reduction in CRR. I could also not vote for tightening to reduce inflation pressures because tightening could not be justified by the already high sacrifice ratios of the ''tightening-quantitative easing'' conundrum (tightening the massive AMCON injections) of the last few years.

I expressed cautious optimism in my personal statement of July 2015 MPC. I remain cautiously optimistic. As I emphasized then, ''policy and strategy should not be based on pessimistic outlooks because nothing in the future is inevitable: ***it is the quality of current choices that will shape future paths.''*** As the new cabinet takes shape, it is important that monetary and fiscal authorities meet as soon as possible to begin the hard-work of designing the appropriate macroeconomic management strategy for Nigeria that builds the resilience, efficiency and effectiveness required to achieve the complementary mandates of the CBN and the fiscal authorities.

I had argued that resumption of refining at full capacity would help to reduce petroleum subsidy payments which will bring about significant reductions in fiscal deficits, public borrowing and public debt and the need for portfolio flows. These changes would significantly reduce the cost of liquidity management, reduce pressures on the forex and money markets and help to bring about improvements in the pricing, allocative, rationing and discovery functions of the money and forex markets. Indeed, improvements in refining and distribution efficiencies could bring to an end the game of petroleum subsidy and its destructive effects on the efficiency and effectiveness of markets and policies (fiscal and monetary).

Similarly, a successful war on corruption would increase government revenue (as leakages and theft are reduced), reduce government expenditure, budget deficit, public borrowing and public debt. These would scale-up the effects of the reduction in petroleum subsidy. The future effectiveness of macroeconomic management in my view hinges strongly on effective and efficient policy coordination. Without that, weathering the inevitable storms of the twin traps will be difficult and very costly. My vote therefore, is for medium to long term efficiency and effectiveness of markets, of macroeconomic management and of the stability of the economy.

## 6.0 NNANNA, O. JOSEPH

Global macroeconomic conditions during Q3 of 2015 were fragile amid financial market uncertainties, softening oil prices and China's uncertain growth future. While advanced economies witnessed gradual improvement in output growth, overall global growth performance was largely uneven across board. In the United States, recent rebound in growth performance was largely driven by continued monetary easing, lower energy prices and improved labour market conditions; while inflation remained far below policy target of 2 percent. However, while marginal deceleration in growth in the Euro Area was attributed to continued fiscal fragilities, slowing growth in emerging and developing economies were mainly driven by economic headwinds, especially lower commodity prices and ripples of growth rebalancing in China.

***OUTPUT AND PRICES***

***While concerns of possible recession and worsening unemployment remain valid given sustained weak output growth, marginal inflation uptick was not surprising, and does not seem to threaten relative price stability in the near term.***

At the domestic front, GDP growth declined from 3.96 percent in Q1 of 2015 to 2.35 percent in Q2, which consequently worsened unemployment from 7.5 percent in Q1 to 8.2 percent in Q2 of 2015. The sustained deceleration in GDP, which stoked fears of recession in the medium term, was largely attributed to softening oil prices, liquidity contraction in the banking sector, dwindling government and private investment expenditure. Overall, broad money supply (M2) declined from 20.64 percent in December, 2014 to -2.23 percent in August 2015, further deteriorated to -3.35 percent (annualized), and compared with the bench mark of 15. 24 percent. Consequently, credit to the private sector significantly contracted from 11.88 percent in December 2014 to 2.80 percent in August 2015. The creeping inflation uptick from 9.2 percent in July to 9.3 percent in August, which was largely driven by food inflation, does not seem to threaten relative price stability. Nonetheless, current monetary conditions and the forthcoming harvest season are expected to dampen threats to price stability in the near term.

### *EXCHANGE RATE DEVELOPMENTS*

***Effective demand management policies in the forex market has halted the hemorrhage in reserves albeit temporarily, but sustained accretion to reserves is threatened by softening oil prices and uncertainties about capital inflows, in the wake of J P. Morgan delisting threat.***

External reserves, which marginally improved from $28.3 billion in June to $31.2 billion in July, remained stable on average at $30.6 billion in August and September 2015, respectively. This underscores the effectiveness of the subsisting demand management policies in Forex market. But challenges of sustainability of the relative stability in reserves remains a major concern. However, while interbank rates remained within the policy band of N197/USD, the BDC rates have significantly depreciated at N224 / USD, with a spread of 13.71 percent between the two market segments. Although, there has been relative stability in reserve levels in recent times, but sustained accretion cannot be assured against the backdrop of softening oil prices and possible portfolio investment reversals due to possible interest rate hike in the US in the near term. In the circumstance, recent developments in the forex market indicate that the combination of strategic intervention in the forex market and sustained demand management policies have the potential to stabilize and possibly improve reserve accretion in the medium term as oil prices unravel and the implementation of structural policies kick in as the new administration stabilizes.

### *LIQUIDITY MANAGEMENT*

***Full implementation of the Treasury Single Account ( TSA) and prevailing tight monetary conditions have impacted credit to the private sector and domestic investments, thus warranting some banking system liquidity accommodation in the short term.***

The combined impact of the Treasury Single Account (TSA) and the 31 percent CRR accounted largely for recent liquidity contraction that depressed credit to the private sector in the period under review. Tight liquidity conditions in the money market caused the rise in interbank and open buy back rates from 10.85 and 10.65 percent to 33.3 percent and 28.10 percent in June and August, 2015, respectively. The relative decline in NPLs from 4.65 percent in June to 4.57 percent in August 2015, in addition to relative stability on return on equity (ROE) and return on assets (ROA), alleys policy concerns about fragilities in the banking system in the near term. However, given the impact of dwindling private sector credit and declining growth in government and private sector investments, there is need for policy to enhance liquidity in the financial sector.

**Conclusion.**

In the light of the mixed signals emanating from macroeconomic developments especially, the uneven growth trends and the decelerating GDP growth at the domestic front, declining credit to private sector, tepid inflationary uptick and weakening government and private sector investment expenditure, I see merit in advocating for:

1. Reducing the CRR from 31 percent to 25 percent;
2. Retain the MPR at 13 percent;

3. Retain the symmetric corridor of 200 basis points around MPR ; and

4. Retain the Liquidity Ratio at 30 percen

## 7.0 UCHE, CHIBUIKE U

Information available to the MPC shows that our local economic environment remains fragile. Given the current downward trend in global oil prices and the dependence of our economy on oil rents, it is not surprising that almost all our economic growth indicators have either stalled or are trending in the negative direction. Our external reserve has stalled while inflation has continued to inch upwards. Our GDP growth rate is on the decline while our industry growth is in negative territory. Although the interbank exchange rate for the Naira has remained stable at N197 to the US Dollar for some time now, the margin between this and the BDC rate has continued to widen. This is a clear indication of the growing pressure on the exchange rate of our currency. The Nigerian Stock Exchange ASI index has, on the average, continued to trend downwards. The recent announcement by JP Morgan to phase out Federal Government of Nigeria Bonds from its Government Bond Index for Emerging Markets by the end of October 2015 has also not helped matters.

The above scenario is clearly a reflection of the mono product dependent nature of our economy. The consequence of our overdependence on oil rents is perhaps best illustrated by the recent mandate given to the CBN to bail out state governments so as to enable them to pay salaries. Bluntly put, states are now borrowing to meet recurrent expenditure. This in my humble view can only complicate our economic problem. Except the states are forced to restructure their operating and cost structures, they will soon come back for more bailout. This is especially plausible given the fact that most analysts have ruled out the possibility of a sustained increase in crude oil prices in the near future.

I do not subscribe to the view that the bail out of states in order to enable them pay salaries can be considered as part of the developmental function of the CBN. For

CBN interventions to be classified as such, it should be focused on the development of real sector economic activities. It is in the light of the above reality that various proposals have been put forward on how the CBN could best aid the economic diversification process. Although I am in support of the CBN exercising its developmental function, I am of the humble opinion that our approach in this direction should be cautious and systematic. Since the CBN has a long history of developmental interventions, I am of the view that we should at the very least first try to learn from history before proceeding. The first thing to do therefore will be to critically study past interventions with the view of understanding their strengths and weaknesses. This I believe will help us design and operationalize better developmental policies for the future. It will also help us to better sequence such developmental interventions.

Despite the gloomy economic picture that may have been painted above, there have been positive economic developments in our country. For me, the most exciting news that preceded this MPC meeting was the decision of the Federal Government to operationalize the Treasury Single Account. In the past, I have consistently argued that the proliferation of the accounts of Government agencies in commercial banks undermines Government fiscal management and the formulation of monetary policy. Such practices have in the past led the MPC to adopt abnormal policies like charging discriminatory CRR on public sector deposits. Unfortunately, such policies have not always proven to be effective.

Although the September 15, 2015 deadline set by Government for the full implementation of the TSA has now passed, data before the MPC shows that thus far less than half of such deposits have been transferred to the CBN. Unfortunately, all manner of claims and counter claims exist, at least in the popular press, with respect to the specific operational modus of the TSA. My interpretation of the present uncertain scenario is that it is only a passing phase that will eventually be sorted out in the near term. Since, in my view, Government is resolute about operationalizing the TSA, I believe it is prudent to wait for the dust to settle before we can determine the full impact of this new policy direction on both monetary policy and the health of banks.

It is on the above basis that I consider the argument that we should reduce CRR in order to give more breathing space to the banks- especially now that their non-performing loans are gradually increasing- hasty. This is even more so given the fact that evidence before the MPC clearly show that thus far, there has been no material decline in the liquidity position of our banks. Rather, a major area of risk for our banks is the increasing foreign currency liabilities in their balance sheets. I am particularly troubled by the fact that some of these foreign currency liabilities are being invested in local currency assets. Thankfully, the current scale of the problem can still be curtailed by proper and effective supervision based on existing standards.

I will like to conclude this statement by commenting on the recent J. P. Morgan decision to delist Nigerian bonds which has been mentioned above. The crux of the matter is the CBN's decision to increase the controls in its foreign currency market. I am in full support of the CBN argument that "given the high propensity for speculation, round tripping, and rent-seeking in the market," the only players who should be allowed are those who are "in the market to fulfil genuine customer demands to pay for eligible imports and other transactions." From the perspective of

Nigeria as the issuer of the said bonds, I am convinced that this is a better arrangement than allowing speculators to determine the value of our currency.

I however wish that the above controls can also be extended to the inflow of capital into the country. Over the years, I have consistently argued that we should do more to regulate this. Surely, it will be more logical and less disruptive to also control the inflow of foreign currency into the country. Foreign capital is useful to the extent that it is invested in productive assets. I humbly do not agree with the argument that this is not the right time to put capital controls in place. To the contrary, I believe that there can be no better time than now that our economy is on the decline. For the avoidance of doubt, capital controls simply means imposing some minimum term limit, perhaps one year, for foreign investments to stay in Nigeria before such investments can be moved without attracting any surcharge. This can also be applied to new inflows only. Under such a scenario, only unwanted speculative foreign investments will leave the shores of our country. Controlling the type of capital we are willing to receive will surely curtail speculative activities in our economy.

In summary therefore, I am inclined to adopt a cautious attitude at the present time. I therefore vote as follows: (1) to retain MPR at 13 percent with interest rate corridor of + 200/- 200 basis points; (2) to retain CRR at 31 percent; and (3) to retain Liquidity Ratio at 30 percent.

## 8.0 YAHAYA, SHEHU

I vote to reduce the CRR to 25% and maintain the current level of MPR along with the asymmetric corridor. The reasoning behind my position is discussed below.

**Global Economy**

There has been little change in the global economic and financial situation since the last MPC meeting. The US, and to a lesser extent Europe, are experiencing economic recovery. Growth is tepid in most of the EU countries and Japan, while India is still growing rapidly. China's growth is still robust but slowing down. Many of the middle-Eastern countries are contending with either conflict or the sharp fall in oil prices. Despite challenges to some major economies in Africa including Nigeria, average growth rates are resilient for the region as a whole.

Oil prices at around $45/bbl remain weak, due to global over-supply, slow growth in most of the OECD countries and rising OPEC production. With low oil prices, softening in the commodity markets, stable food production, prices are low in most of our major trading partners, while a few are facing deflationary pressures. Stock prices have generally been experiencing downward pressures or significant volatility. The US Dollar has appreciated against most major currencies. US Federal Reserve have maintained interest rates at the current rate

**Domestic Economy**

During Q2 2015, the GDP growth rate in the country fell significantly to 2.35%, with projections for the year ranging from 2.5% to 5%, compared to 3.96% in the Q1 2015 and 6.33% in 2014. In addition to declines in the oil sector, manufacturing production has been particularly hard hit, with a fall of 3.12%. This level of slow-down may have significant implications for job creation and the financial sector. Already, unemployment has edged up to 8.2% and underemployment to 18.3%, compared to 7.8% and 17.5% respectively in 2014.

Prices for Nigeria's Bonny light crude has fallen to $47/b by August 2015, lower than it had been for months, while output has remained stable or slightly higher. Both price and output are currently well below the budget projections, with implications for government revenue,, foreign reserves, forex market, government expenditure, particularly capital expenditure.

Consequently, domestic general price levels have continued their upward trajectory, with headline inflation at 9.34%, core inflation rising faster than food inflation

The exchange rate has, due to administrative measures implemented, remained stable at the inter-bank market. Nevertheless, some pressure has clearly built up on the value of the Naira, mainly due to the low earnings from oil. External Reserves, although have experienced some decline, but remain at a healthy level.

Aggregate credit to the economy slowed down, although credit to government exploded by more than 150% in July 2015. This is partly a reflection of the drastic reduction of about 30% in the distribution of the revenue account in January-August 2015 compared to the same period in 2014. However, actual federal government expenditure in the first half of 2015 was significantly higher than expenditure in the corresponding period of 2014, despite the sharp fall in revenue

The banking system remains in good health with respect to capital adequacy, liquidity, NPLs. Profit levels have increased significant by about 28% in Q2 2015. There are a few challenges though, with respect to the possible consequences of the implementation of the TSA, the fall in oil prices as it relates to the general business climate, some asset/liability mismatches and the relative concentration of the loan portfolio. These are being addressed

**Conclusion**

The MPC is confronted with the three challenges of a sharp fall in the GDP growth rate, rising inflation and pressures on the foreign exchange market. Another challenge is the possible effect of the full implementation of the TSA on liquidity in the banking system. The challenges in the foreign exchange market are being vigorously tackled and stability has been restored there so far. On the TSA, the effects on the banking system have been muted so far. However, rising inflation poses challenges for the economy. Yet, it may be inappropriate to tighten monetary policy at this stage, when growth is slowing sharply and when the effects of the TSA have clearly not fully played out. Indeed, some loosening might be called for to help stimulate economic activity and encourage the banking sector to lend more to the productive sectors. This would be an appropriate corollary to the policies implemented by the central bank to re-align the allocation of foreign exchange.

I therefore vote to maintain the MPR at the current level and to reduce the CRR to 25% to provide additional room for Bank lending. Incentives should be provided to the DMBs to use the additional lending space to support key productive sectors of the economy with the aim of strengthening import substitution, local value-addition and the creation of jobs. This will of course work only if implemented in conjunction with an enabling fiscal policy environment.

### 9.0 ADEDOYIN SALAMI

September's meeting of the Monetary Policy Committee (MPC) concluded with the majority of members voting to reduce the Cash Reserve Ratio (CRR) from 31percent to 25percent whilst maintaining the status quo on all other policy instruments. I was in the minority of members unable to support the proposal to reduce CRR. I voted to maintain the status-quo on all policy parameters including the CRR, primarily because of what I considered to be an inappropriate use of the CRR.

The proposal by Bank Staff for lowering CRR hinged on the following: (i) alleviate the difficulty being experienced by banks in adjusting to implementation of the Treasury Single Account (TSA) Policy; (ii) addressing the deteriorating economic conditions - especially slowing output growth; and (iii) preparing for the effect of exit from the JP Morgan Index.

Presentation by Bank Staff had flagged the need to alleviate problems being experienced, or anticipated, by banks that were finding it difficult to replace public sector deposits lost to the Federal Government's Treasury Single Account (TSA) directive. The consequent loss of funding resulting from TSA implementation would make it difficult for the affected banks to retain assets on their balance sheets. Indeed, ahead of the deadline for compliance with TSA, overnight rates in the interbank market rose from 6.7percent on 14th September to 91percent by the close of the market on deadline day.

The Bank also sought to promote market conditions that would enable banks to relax the terms of deteriorating loans in sectors directly affected by continuing effects of oil revenue shocks to the economy. At issue here is the longer duration of finance expected to support credit restructurings increasingly sought by the large borrowers – especially sub-national governments, and borrowers in Energy and Manufacturing sectors. A concern was also raised about the need to enhance liquidity as we approach the final acts of Nigeria's exit from the JP Morgan GBI EM. As I noted earlier, the majority of Committee members were persuaded to reduce the CRR from 31% to 25% of deposits. However, I was not persuaded that the policy proposal constituted an appropriate response to the characteristics of the Economic Environment as presented by available data.

The liquidity issues we deliberated on appear to me to be specific to a particular cohort of banks, and were not systemic in nature. Data provided show that the liquidity ratio for 8 banks exceeds 50percent. 2 other banks have liquidity ratio of between 40 and 50percent. A further 3 banks reported liquidity ratio of between 35 and 40percent. In other words, half of the Deposit Money Banks attained liquidity levels significantly higher than the prescribed minimum. I must immediately concede that in the absence of data to identify the various banks, our hope must be that the banks close to the regulatory minimum are not systemically important.

I also note that the 'spike' in interest rates around the deadline for TSA implementation was corrected within a few days. The short-lived increase may simply be the result of uncertainty as to how much Federal Government deposits would be affected. Strangely, notwithstanding rising interbank rates, the CBN 'Repo' window remained unused.

Given my view that the liquidity issues relate only to particular banks, it is inappropriate to deploy the Cash Reserve Ratio (CRR) that, as a tool is non-discriminatory and thus cannot address bank-specific liquidity problems, it is, in my view, thus inappropriate to deploy. Furthermore, while a one-time injection of liquidity may enable banks to retire expiring payment obligations, it offers no help in extending maturities of their funding liabilities.

While some, but not all, banks were experiencing liquidity problems as a result of TSA enforcement. The MPC's decision, in my view reflects understandable desire to have the Central Bank relieve pressure-points of banks feeling the pinch. However, rather than directly targeting liquidity to those institutions needing it most, the implication of the MPC's decision is, in effect, to flood the market. Reduction in CRR, will release approximately 750-800 billion Naira – a magnitude of liquidity that seems more appropriate for responding to a financial crisis.

My view is that there is no existential crisis; just a number of poorly run banks, with weak treasury operations, that have been caught out by the inevitable consequence of relying on highly concentrated depositor bases for funding. This last point being a pre-existing condition in the system that we have all been well-aware of. Hence, the solution proposed by Bank Staff is uncharacteristically imprudent especially as nothing in the available data indicated any lack of suitable collateral against which the Bank could have directly, targeted the required relief.

Evidence presented to the Committee showed that TSA related withdrawals amounted to approximately NGN400bn, one-third of the Federal Government's NGN1.4trn deposits. The CBN therefore sought to re-inject almost double the amount of liquidity it had drained into the TSA. However, even without this measure, practically all banks continued to meet, and most even exceeded, the CBN's minimum liquidity ratio - currently 30% of deposits. Indeed, at 40.65%, the average liquidity ratio of banks after commencement of TSA implementation is only marginally worse than the 41% level reported, in June.

I had been concerned about the likely impact on yields of Nigeria's exit from the JP Morgan GBI EM when the exit process is completed before our next meeting in November. My key fear being a rise in yields if banking sector liquidity is inadequate to cope with sales by departing investors. Available information suggests that the size of sales by departing investors is unlikely to significantly exceed US1bn. At this level, the impact on bond market yields is nothing to be concerned about. Overall, I found the arguments advanced to be largely unsupported by available data. I thus felt that deploying the CRR against our stated goals would be a misapplication of this policy tool. I therefore cast a dissenting vote against its reduction.

My skepticism about the liquidity challenge is further strengthened by the absence of an untoward surge in the level of Non-Performing Loans (NPLs) that might have caused a loss of funds from the banking system. Indeed, the latest available reports showed August NPLs, at 4.56% in August 2015, to be improving over the position of 4.65% of loans reported, for June 2015, at our last meeting.

Furthermore, inflation still appeared to be on the upswing – albeit at a slowing pace; continuing to remain outside the desired 6-9% band. At 9.3%, Headline Inflation is at its highest level since May 2013. The CBN's staff forecast suggests that Headline Inflation is likely to peak at 9.4% in September, ease to 9% in November, before ending 2015 at 9.2%.

Beyond inflation, data presented confirmed a sharp slowing in output growth. Gross Domestic Product (GDP) in Q2-2015 showed output growth to have diminished to 2.35percent from 3.96percent the previous period. Detailed review of figures provided by the National Bureau of Bureau (NBS) affords a graphic view of the nature of the slow-down in output growth. Less than 5% of the economy grew faster in Q2-2015 than in the same period a year ago. A further 73.5percent, though still continuing to grow, is growing significantly less rapidly than had been in Q2-2014. The remaining 21.7percent of the economy are now shrinking. With unemployment and underemployment rising to 8.2precent and 18.3percent in Q2-2015, it is clear that the effect of slowing economic activity is translating into rising joblessness!

The case that the extra stimulus of liquidity from reducing CRR would boost credit provision to the real sector is also, in my opinion, not valid. This argument is, in my view, fatally undermined by evidence provided showing banking industry loan-to-deposit ratio is just short of the 80% limit stipulated by prudential guidelines. Given my analysis of available data, my expectation is for the additional liquidity, whilst reducing bond yields, may also worsen forex market conditions.

From a Macro-economic viewpoint, the proposal to lower CRR is inconsistent with the economic characteristics to which the evidence of data provided attests. The economy is obviously struggling to overcome demand-side constraints compounded by an exchange rate policy, which hampers capacity utilization. As the Statistician-General made clear in his comments, rising unemployment and under-employment coupled with the non-payment of public sector salaries have weakened demand. Indeed, it would appear that the NGN338bn 'bail-out' afforded State governments through restructuring of loans has had, at best, a marginal impact on the ability of this tier of government to meet its payroll obligations – especially arrears. Banks, it would appear, have been the primary beneficiaries of that exercise!

At this stage, without further adjustments to relative prices in the economy, it is doubtful that any supply-side boost will benefit the real sector. With its supply chains disrupted, end-user markets contracting, and cashflows drying up, much of the real sector is losing the ability to sustainably utilize, much less attract, financial sector liquidity. The impact of the decision to provide additional liquidity in these circumstances is more liable to stagnate in financial institutions than flow towards the real sector. Such measures of size will more likely inflate Naira fixed income and currency asset prices, rather than improve growth and employment prospects of the economy.

None of the issues that need to be addressed will, in my opinion, be remedied by the reduction in CRR. In other words, the accommodative policy stance that was certain to ensue, nothing in the data warranted policy easing at this time.

Looking ahead, it is clear that the nettle of adjustment to low and uncertain oil price remains to be grasped. The task of defining and treading a strategic path for monetary, fiscal and regulatory policy should become easier with completion of the on-going process composing the government.

## 10.0 EMEFIELE, I. GODWIN, GOVERNOR OF THE CENTRAL BANK OF NIGERIA AND CHAIRMAN, MONETARY POLICY COMMITTEE

Encumbered by weak demand, the global economy faltered in the first half of 2015 and lost some momentum as near-term growth prospects dimmed. Though projected global growth for 2015 broadly remained within 3.0–3.5 percent, the OECD Interim Economic Outlook for September 2015 revised growth forecasts downward by 0.1 percentage point. Global growth performance remained asymmetric across countries and largely reflects the outcomes in key advanced economies. Buoyed by softening commodity prices, recovery and prospects, steadied in major advanced economies in contrast to many emerging and developing economies where the outlook worsened further. While cheaper commodity prices are expected to boost global economic activities in the short-term, the drag from the adverse effects on the economies of commodity exporters may outstrip the benefits to importers.

Among developed countries, recovery in the United States remained on track with a better than envisaged growth in 2015Q2. This reflected a gradual cyclical recovery, the momentum of which may be impeded in the rest of the year due to strengthening dollar. However, in adjoining Canada, the growth estimate was lowered due to further downgrades of business investment plans in the energy sector and slowing exports of non-energy allied goods and services. In the UK, growth trajectory is expected to foster in 2015; supported by strong real income growth, accommodating credit conditions, and elevated business and consumer confidence. In the Euro area, though growth is slower than expected, recovery and prospect in the region continue to improve. The sustained recovery observed in some advanced economies is underpinned by improving financial conditions and consumer sentiments, favourable labour market conditions, growing private consumption due to the positive impact of softening energy prices on real income growth. Growth recovery and prospects among advanced economies was reinforced, among others, by the deferral of interest rate adjustment in the United States and the prevailing asset purchase programmes of the European Central Bank, the Bank of England and the Bank of Japan.

I note that the tepid economic growth observed in emerging and developing economies in the first half of 2015 is expected to carry on for the remainder of the year and into 2016. For 2015, the group's growth outlook is projected to slow to 4.3 percent due to weakening demand, falling commodity prices, structural imbalances, non-accommodating monetary policy, and intensifying vulnerabilities. These vulnerabilities are underlain by harsher than anticipated slowdown in the Chinese economy where weakening export is dragging growth potentials below its long-run trend. Though the Chinese economy grew by 7.0 percent in 2015Q2, it is projected to slow to 6.8 percent at the end of 2015 from 7.4 percent in 2014. The faltering growth in China stoked the prevailing financial turbulence in the economy with a considerable pull on the short-term prospects of the global economy. Other important emerging and developing countries, especially, Russia and Brazil are also experiencing profound contractions which are in some cases accompanied by higher than average inflation rate while India is projected to continue to grow strongly. For low-income developing countries and the sub-Saharan region, growth prospect remain weak with a projected deceleration of 0.5 percentage points apiece in 2015 to 5.5 percent and 4.5 percent, respectively.

The slight ease in the threats of deflation among major advanced economies notwithstanding, inflation rate remained very low in these economies keeping the expected global inflation in 2015 relatively moderate. This reflected the continued softening of energy prices, nominal wage rigidities and weak global demand. Among emerging and developing economies, disinflation is gathering pace in commodity importing countries due to the cushioning effects of lower energy and commodity prices. Commodity exporting emerging and developing countries, including Brazil and Russia are experiencing intensifying uncertainties and inflation volatility as domestic prices are ascending sharply following escalating imbalances in their foreign exchange markets and fiscal positions.

In Nigeria, growth prospects for 2015 weakened following the slowing growth observed in the first two quarters of the year. Output growth decelerated from 3.9 percent in 2015Q1 to 2.4 percent in 2015Q2 which was considerably less than the 6.5 percent and 6.2 percent recorded in 2014Q2 and 2014Q4, respectively. Consequently, the annualised growth projection for 2015 has been marked down from 5.5 percent to 2.6 percent. The fragile performance of the economy in the second quarter of 2015 reflects the sustained turmoil in the oil sector caused by tumbling crude oil prices which led to a 0.7 percent decline in oil related GDP. However, the positive growth in output during the quarter was driven essentially by a 3.5 percent expansion of non-oil GDP. This was underpinned by the services, trade and agriculture sub-sectors which jointly contributed over 90 percent to the overall growth.

I note that the sub-par performance of the economy in the second quarter is not unique to Nigeria, but continue to reflect the imbalances and vulnerabilities inherent in commodity exporting economies. Nevertheless, it highlights the immediate need for fiscal consolidation and an accelerated diversification of the economy. The easing infrastructural challenges illustrated by the increased availability of petroleum products (especially premium motor spirit), improved power supply and the gradual dismantling of insurgents in the North east region can possibly prop the faltering prospects in the short-term. In addition, the initial frictions that followed the prohibition of non-essential imports from the foreign exchange market are dissipating as domestic supply capacity is beginning to improve. This has the potential to strengthen the short- to medium-term economic prospects.

On domestic consumer prices, the year-on-year rate of headline inflation stayed above the Bank's tolerance range of 6—9 percent, although it remained single digit. The August 2015 Consumer Price Index report of the National Bureau of Statistics indicated that gradual rise in inflation rate was sustained as the rate increased slightly from 9.2 percent in July to 9.3 percent in August. Accordingly, inflation rate has increased for nine consecutive months. The rise in headline inflation in the review month derives from the ascent in both the core and food components of inflation. Core inflation quickened 18 basis points to 9.0 per cent in August while food inflation, at 10.1 per cent, added 8 basis points. The continued creep in inflationary pressure is attributable to the base effects resultant from unfavourable energy prices and exchange rate pass-through, which may have been exacerbated by delayed harvests. The ramification of the base effect is buttressed by the renewed slowdown in the month-on-month rate of inflation. In the review month, month-on-month rate of headline inflation decelerated by 10 basis points to 0.59 percent, food inflation dropped 14 basis points to 0.63 percent, whereas core inflation remained unchanged at 0.61 percent. Though reflective of the legacy effects of the uncertainties that pervaded the economy early in 2015, the rising inflationary pressure remained effectively underpinned by both structural and cyclical factors. The moderating fear of deflation in key advanced countries and a strengthening dollar heighten the upside risks of imported inflation in short-term, especially in the backdrop of relatively tight monetary conditions.

Liquidity conditions in the domestic monetary, credit and financial markets remained tight as broad money supply (M2) declined by 2.2 percent in August 2015 from the end-2014 level. This represented a sub-par annualised contraction of 3.3 percent in contrast to the 15.2 percent expansion targeted for 2015. The decline in money supply during the month was attributable to the outcomes of net foreign assets. On the contrary, net domestic credit recorded an 11.0 percent expansion in August, which translates to annualised growth of 16.5 percent relative to the programmed target of 29.3 percent in 2015. This growth was largely driven by elevated claims on federal government, which grew by 140.1 percent during the review period.

The lingering tight liquidity conditions reflected in the money market where interest rates were relatively volatile. Average interbank call and the OBB rates rose sharply from 10.9 and 10.7 percent, respectively, in June 2015 to 31.1 and 28.1 percent in August 2015. Cumulated for that period, interbank call and the OBB averaged 14.9 and 17.1 percent, respectively. At the equity segment of capital market, conditions remained bearish in the review period. The All-Share Index, closing at 30,332.7 points on 18 September 2015, shed 9.3 percent from the 33,456.83 points recorded at the beginning of June 2015 while market capitalisation, at ₦10.4 trillion, decreased by 8.8 percent. Year-to-date, both All-Share Index and market capitalisation have lost 12.5 and 9.3 percent of their respective values. The fragility in the capital market is due essentially to the insipid investor sentiments that accompanied the 2015 elections and the sustained uncertainties associated with the uncomplimentary dynamics of external reserves and crude oil prices.

I note the continued dissimilar outcomes in the two segments of the foreign exchange market in the review period. At the interbank market, the exchange rate was relatively stable with a daily average rate of ₦196.95/US$ between 29 June 2015 and 18 September 2015 and a depreciation of ₦0.05k to close at ₦197.00/US$. On the other hand, the bureau de change segment of the market recorded a ₦13.00 appreciation, opening at ₦224.50/US$ and closing at ₦211.50/US$. The non-negative outcomes in both segments reflect the continued resolve of the CBN to ensure stability in the market using both administrative procedures and policy actions. This notwithstanding, exchange market pressure persists as the gross official reserves declined comparatively by 1.8 percent to US$30.6 billion as at 17 September from US$31.2 billion in July 2015.

In general, given current macroeconomic conditions, I believe that countervailing measures are immediately needed to act as a fillip to the growth. The weakening economic growth is traceable to the waning aggregate demand following the diminished government expenditure and weak private consumption. The combination of rising prices and falling expenditure is essentially reflective of an aggregate supply imbalance and critically underscores the exigent need to diversify the economy and ensure that domestic supply capacity is bolstered. Against this backdrop and given that the overbearing source of the present economic fragility – i.e. oil price decline – is exogenous, I reiterate the imperatives of a coordinated synergy of fiscal and monetary policies as the panacea that will reposition Nigeria in the aftermath of the prevailing unsavoury conditions.

On the financial system, I recognise that following the implementation of the TSA, liquidity condition in the system may need to be eased creatively in a way that concurrently strengthens financial system fundamentals and directs the flow of vital credit to the productive sectors of the economy. Given the lingering demand pressure in the foreign exchange market and the firm resolve of the CBN to maintain exchange rate stability despite the pressures, it is crucial to ensure that any extra liquidity released into the system is not re-routed to the FX market but channelled to growth generating ventures and enterprises. I therefore call for increased lending to the MSMEs, agriculture and manufacturing sectors as these have the capacity for output enhancement, employment generation, wealth creation and poverty reduction.

While I appreciate the counteracting effects of crude oil receipts on fiscal balances, rising credit to government and the flagging debt profile, I urge the relevant fiscal authorities to direct effort at capital undertakings in power, energy and transportation which could immediately bolster the domestic economy. I am of the opinion that, as the economic blueprints of the government become clearer, uncertainties will dissipate, financial markets will steady, business outlooks and consumer sentiments will improve, productive capacity will strengthen, and domestic inflation will moderating. I acknowledge that the recent decisive action to clear accumulated salary arrears owed civil servants at sub-national levels would bolster private consumption and growth prospects in the near-term. Nonetheless, I remain strongly resolute that, even in the face of rising inflation, some form of expansionary monetary policy is needed to support the economy, promote growth and enhance job creation at this critical time.

It is against this backdrop that I vote as follows:

1. Reduce the CRR from 31 to 25 percent;
2. Retain the MPR at 13 percent;
3. Maintain a symmetric corridor of ±200 basis points around the mid-point of the MPR; and
4. Maintain the Liquidity Ratio at 30 percent.

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