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Calling Legislative attention to salient issues arising from the CBN Monetary Policy Committee meeting of 25th and 26th March, 2019

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Executive Summary

This brief calls for legislative attention to salient issues arising from the CBN Monetary Policy Committee meeting of 25th and 26th March, 2019. Among the key issues considered are; Domestic Output Developments and Developments in Money and Prices. The brief recommended the following to the Legislatures;

- The Central Bank of Nigeria should reduce the Monetary Policy Rate (MPR) (to a single digit level) in the next Monetary Policy Meeting. This will boost the Net Domestic Credit and in turn ease the private sector borrowing cost.
- NASS relevant committees should ensure that there is proper alignment and coordination between monetary and fiscal authorities in the areas of policies and programmes. For instance, the FGN's target of job creation does not align with the CBN tight monetary policy stance, particularly with the high MPR and CRR.
- The National Assembly should engage the Central Bank to ensure that it effectively performs its monitoring and supervisory function to the deposit money banks.
- The National Assembly should ensure that the CBN upholds its commitment to promoting strong growth by way of encouraging credit flow to the productive sectors (especially the non-oil) of the economy.
- Express legislative attention should be accorded to Bills that have the potentials to support the manufacturing and service sectors so as to sustain the current growth witnessed in the sectors.
- CBN's interventions in the real sector as well as the implementation of the Economic Recovery and Growth Plan (ERGP) by the Federal Government has been adjudged to be working by the MPC. There is need for legislative support to these laudable initiatives, mainly, through innovative legislations and oversight.
- Given that rebasing the GDP will, at least, make planning and investment decisions more robust, NASS should support every effort in that regard.

I. Overview

The Monetary Policy Committee (MPC) met on the 25th and 26th March, 2019; against the backdrop of developments in the global and domestic economic environments in the first quarter of 2019. The Committee noted with concern the weakening performance of global output growth at the end of 2018 and observed that developments in the first quarter of 2019 were characterized by legacy headwinds from the second half of 2018. These include: the continued trade war between the US and China, policy uncertainty amongst advanced economy central banks; persisting uncertainties surrounding BREXIT negotiations; vulnerabilities in major financial markets and rising public debt in some Emerging Markets and Developing Economies (EMDEs). Consequently, global output growth for 2019 was downgraded by the IMF from 3.7 per cent to 3.5 per cent.

1.1. *Domestic Output Developments*

Output data from the National Bureau of Statistics (NBS) indicate that real Gross Domestic Product (GDP) grew by 2.38 per cent in Q4 2018 from 1.81 and 2.11 per cent in the previous quarter and corresponding period of 2017. The major impetus for growth came from the non-oil sector, which grew by 2.7 per cent in Q4 2018, while the oil sector contracted by 1.62 per cent. The MPC welcomed the continued positive sentiments in the Manufacturing and Non-Manufacturing Purchasing Managers' Indices[1] (PMIs) for the 23rd and 24th consecutive months in March 2019. The manufacturing PMI rose by 57.4 index points compared with 57.1 in the previous month. Similarly, the nonmanufacturing PMI increased by 58.5 index points compared with 58.4 in February 2019. The increase in both measures of PMI was driven by increases in production, employment, raw material inventories and new orders. This improved outlook was attributable to the continued stability in the foreign exchange market, various interventions by the CBN in the real sector and the effective implementation of the Economic Recovery and Growth Plan (ERGP) by the Federal Government. Further, on the current measure of national output, the MPC noted the need to rebase the GDP, an exercise which was last carried out in 2010.

Why the Legislature should support the rebasing of the GDP

Gross Domestic Product (GDP) is an internationally recognized measure of an economy's size and strength. It is important to have up-to-date data, so the rebasing is a step in the right direction. It is expected to make planning and investment decisions more robust and informed. For instance, the performance of Nigeria in revenue collection, capital spending, external debt and budgeting can be benchmarked against its contemporaries. Not rebasing is like a farmer who breeds animals but had not properly counted his animals in the past. GDP rebasing will help to stimulate the economy and introduce new optimism to investors in particular and the entire citizens in general.

1.2. *Developments in Money and Prices*

The Committee noted that broad money supply (M2) contracted by 1.98 per cent in February 2019, below its level at end-December 2018. Net Foreign Assets (NFA) contracted by 7.47 percent in February 2019 relative to its level at end-December 2018. In contrast, M3 grew by 4.31 per cent in February 2019 compared with its level at end-December 2018. Net Domestic Credit (NDC) also grew by 10.68 per cent in

[1] The Purchasing Managers' Index (PMI) is an indicator of economic health for manufacturing and service sectors. The purpose of the PMI is to provide information about current business conditions to company decision makers, analysts and purchasing managers.

February 2019. The growth in NDC was accounted for by the increase in credit to Government which grew by 17.20 per cent in February 2019 over its level at end- December 2018. Credit to the private sector also rose by 6.41 per cent compared with its growth benchmark of 9.41 per cent. Given the positive trajectory, the Committee urged the Management of the CBN, to sustain the various initiatives of the Bank, particularly the partnership between the Bankers Committee and the Nigeria Incentive-Based Risk Sharing System for Agricultural Lending (NIRSAL) aimed at establishing a national microfinance bank to cater for the MSMEs of the economy.

The Committee observed the continued moderation in inflation as headline inflation (year-on-year) declined further to 11.31 per cent in February 2019 from 11.37 and 11.44 per cent in January 2019 and December 2018, respectively. The decrease in headline inflation was driven mainly by food inflation, which declined to 13.47 per cent in February 2019 from 13.51 per cent in January 2019, while core inflation declined marginally to 9.80 per cent from 9.91 per cent in the previous month. On a month-on-month basis, headline, food and core inflation declined to 0.73, 0.82 and 0.65 per cent in February 2019, respectively, from 0.74, 0.83 and 0.81 per cent in January 2019. The Committee noted the upside risks[2] to inflation to include; high cost of energy, infrastructure constraints, insecurity in some parts of the country; and anticipated increase in liquidity from the late implementation of the 2018 budget, and noted that most of these factors were outside the ambit of monetary policy. The MPC, therefore, urged the Federal Government to sustain its current effort in stimulating output growth by executing the policies approved in the ERGP.

The Committee noted with satisfaction, the continued stability in the foreign exchange market at the Investors' and Exporters' (I&E) window of the market. In particular, it observed the moderate improvement in oil prices and stable accretion to external reserves, which stood at US$45.2 billion as at March 21, 2019, a 6.73 per cent increase from US$42.35 billion at end-February 2019.

2. Analysis of the developments in Money and Prices

The increase in broad money supply (M3) by 4.31 per cent in February 2019 compared with its 1.98 per cent contraction as at end-December 2018 indicates that the economy is indeed on the growth path. An increase in supply of money typically lowers interest rates, which in turn, generates more investment and puts more money in the hands of consumers, thereby stimulating spending. Businesses respond by ordering more raw materials and increasing production. More so, Net Domestic Credit (NDC) is growth inducing. There is emerging consensus among economic scholars that private sector credit impacts positively on economic growth.

In addition, the CBN's Consumer Expectations Survey for December 2018 which shows that consumers expect inflation rates to rise in the next 12 months, potentially driven by increases in rent, food prices, electricity tariff and prices of other household items was not confirmed, at least, for now. However, looking at the consistent decline in inflation rates from 18.55% in December, 2016 to 15.37% in December, 2017 and 11.37% in December, 2018, the target inflation rate of 9.98% in the 2019 budget may be realizable if the CBN maintains its current policy stance.

[2] Factors which can pull the inflation up

3. What Legislatures should do

- Although it was noted that credit to the private sector rose by 6.41 per cent, most of the money deposit Banks are still not providing low priced credit to the sector, particularly small and medium size businesses in the manufacturing sector that has capacity to generate jobs. The reason for the high cost of credit is not far-fetched. It stems from the harsh business environment that banks operate which is characterized with high risk and high operational cost. Monetary Policy Rate of 13.5% agreed upon by the MPC in its March meeting which is still on the high side couple with the current double digit inflation rate (11.31%) is another major problem confronting businesses in the private sector. Such Businesses would find it difficult to thrive under this kind of condition and new businesses may not have access to startup capital from the formal financial sector.
- It therefore becomes imperative that the legislature through the instrumentality of the budget, appropriation and oversights functions ensures that the capital expenditure component of the budget, particularly on infrastructure such as roads, rail and electricity are implemented effectively and efficiently. The issue of security equally requires attention. The infrastructure and security costs are part of major cost borne by most money deposit banks that add up significantly to their cost of borrowing. Starting from the 2019 budget, the legislature should do critical review and appraisal of budgetary provision for infrastructure, monitor and carry out effective oversights on the various infrastructural projects such that the infrastructure deficit in the country can be reduced. Banks can then operate with minimal cost and the cost of borrowing may reduce. Businesses may then have access to cheap credit from money deposit banks to finance their plans. The Central Bank of Nigeria should consider reducing the MPR to a single digit level and the Cash Reserve Ratio in the next Monetary Policy Meeting. This will go a long way to boost the Net Domestic Credit and in turn ease the private sector borrowing cost.
- There is need for proper alignment and coordination between monetary and fiscal authorities in the areas of policies and programmes. The Economic Recovery and Growth Plan (ERGP), Medium Term Expenditure framework (MTEF) and Fiscal policy strategy paper of the Federal Government and other policy actions should be aligned with the CBN policies and actions. Most often, monetary and fiscal policies are at variance. For instance, the FGN's target of job creation does not align with the CBN tight monetary policy instance particularly high MPR and CRR. The policy of CBN and FG through the Budget and Planning and Finance ministries should be well coordinated. The Legislature may initiate a Bill for an Act that requires proper coordination between the monetary authority and the Fiscal authority to prevent them from working at cross purposes. This will go a long way to create policy consistency and help develop the real sector of the economy.

- Credit to the private sector though rose by 6.41 per cent fell short of its growth benchmark of 9.41 per cent. Among the possible reasons for this is that the Central Bank appears not have been doing enough to monitor and supervise the deposit money banks. The National Assembly may need to engage the Central Bank in this regard as current report from NDIC indicates that there is high non-performing loans in the various Banks and these loans are traceable to Directors of Banks as part of insider abuse. Assuming the Central Bank surveillance and monitoring has been effective, the loans may have been channeled to the real sector where they may be used more productively.
- The National Assembly should ensure that the CBN upholds its commitment to promoting strong growth by way of encouraging credit flow to the productive sectors (especially the non-oil) of the economy.
- Express legislative attention should be accorded to Bills that have the potentials to support the manufacturing and service sectors so as to sustain the current growth being witnessed in the sectors.
- CBN's interventions in the real sector as well as the implementation of the Economic Recovery and Growth Plan (ERGP) by the Federal Government has been adjudged to be working by the MPC. Legislatures should support these laudable initiatives through innovative legislations and oversight.
- Given the obvious benefit inherent in rebasing the GDP, NASS should support every effort in doing so.
- Despite the good outlook for inflation, the Federal Government should ensure that the level of insecurity all over the country is brought under control.
- The recent call by the IMF for the removal of oil subsidy should be handled with caution. Removal of subsidy without alternative efficient welfare package might spell doom.
- The MPC did not take into cognizance the inflationary pressure the implementation of the new minimum wage will generate. NASS should call on the NPC to demonstrate how the effects of such pressures will be mitigated vis-à-vis the inflationary target of the 2019 budget.

4. Conclusion

This brief calls for legislative attention to salient issues arising from the CBN Monetary Policy Committee meeting of 25th and 26th March, 2019. Among the key issues considered are; Domestic Output Developments and Developments in Money and Prices. The brief recommended the following to the Legislatures;

- The Central Bank of Nigeria should reduce the MPR (to a single digit level) in the next Monetary Policy Meeting. This will go a long way to ease the private sector borrowing cost and in turn boost the Net Domestic Credit.
- NASS relevant committees should ensure that there is proper alignment and coordination between monetary and fiscal authorities in the areas of policies and programmes. For instance, the FGN's target of job creation does not align with the CBN tight monetary policy stance, particularly with high MPR and CRR.
- The National Assembly should engage the Central Bank to ensure that it effectively performs its monitoring and

supervisory function to the deposit money banks. Although Credit to the private sector rose by 6.41 per cent, it fell short of its growth benchmark of 9.41 per cent. Thus indicating that more monitoring and supervisory role is required.

- The National Assembly should ensure that the CBN upholds its commitment to promoting strong growth by way of encouraging credit flow to the productive sectors (especially the non-oil) of the economy.
- Express legislative attention should be accorded to Bills that have the potentials to support the manufacturing and service sectors so as to sustain the current growth being witnessed in the sectors.
- CBN's interventions in the real sector as well as the implementation of the Economic Recovery and Growth Plan (ERGP) by the Federal Government has been adjudged to be working by the MPC. Legislatures should support these laudable initiatives through innovative legislations and oversight.
- Given the obvious benefits inherent in rebasing the GDP, NASS should support every effort in that regard.

The views expressed in this Research Issue Brief are those of the author(s) and do not necessarily represent the views of the Institute and its Management.

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