CENTRAL BANK OF NIGERIA

MONETARY POLICY REVIEW

FEBRUARY 2018

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Central Bank of Nigeria

Mandate

▪Ensure monetary and price stability

▪Issue legal tender currency in Nigeria

▪Maintain external reserves to safeguard the international value of the legal tender currency

▪Promote a sound financial system in Nigeria

▪Act as banker and provide economic and financial advice to the Federal Government

Vision

“Be the model Central Bank delivering Price and Financial System Stability and promoting Sustainable Economic Development"

Mission Statement

“To be proactive in providing a stable framework for the economic development of Nigeria through effective, efficient and transparent implementation of monetary and exchange rate policy and management of the financial sector"

Core Values

- Meritocracy
- Leadership
- Learning
- Customer - Focus

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STATEMENT BY THE GOVERNOR

The monetary environment in the second half of 2017 was characterized by several challenges on both the global and domestic fronts. Although the global economy continued on its recovery path, the continued slow pace of recovery in crude oil and other commodity prices, reduction in China's uptake of global commodities and financial market uncertainties due to reduced pace monetary policy normalization in the US, the BREXIT negotiations, as well as trade protectionism and immigration challenges, were key risks to the recovery efforts. Notwithstanding these threats from the external sector, the domestic economic environment witnessed further improvement reflected by stability in the foreign exchange market, buoyed by rising oil receipts and growing external reserves as well as the implementation of the Economic Recovery and Growth Plan (ERGP). Consequently, the economy grew by 1.40 per cent in the third quarter and further by 1.92 per cent in the fourth quarter of 2017. These were significant expansions in contrast to the contractions of 2.34 and 1.73 per cent in the respective quarters 2016. The improved performance in the review period was attributed to the growth of both the oil and non-oil sectors. Overall, the economy grew by 0.83 per cent in 2017, reversing the contraction of 1.58 per cent in 2016. The development was attributed to several factors, including the moderate rise in crude oil prices and improvement in oil production following the relative peace in the Niger Delta region.

On the general price level, the sustained the implementation of existing measures on foreign exchange management including the newly introduced Investors' and Exporters' (I&E) window, special foreign exchange auction to targeted sectors, as well as foreign exchange sales for small scale importation, led to stability in the foreign exchange and with lower pass-through from import prices to inflation. In addition, the sustained non-accommodative monetary policy stance helped to rein-in inflationary pressure in the review period. As a result headline inflation continued to moderate from 16.05 per cent in July to 15.37 per cent in December 2017.

The Bank sustained its tight monetary policy stance and continued to employ various policy instruments in its tool kit in the review period in order to achieve the objective of price and macroeconomic stability. The MPR was maintained at 14.0 per cent throughout the period along with the asymmetric corridor of +200 and -500 basis points around the MPR. The Bank also increased its reliance on Open Market Operations (OMO) as the main tool for managing banking system liquidity in the second half of 2017. This was complemented by foreign exchange interventions, as necessary. The Nigerian capital market remained largely bullish in the review period, reflecting investor positive sentiments as macroeconomic conditions improved. The sustained tight monetary policy stance of the Bank improved returns on domestic assets and attracted foreign inflows into the capital market. Consequently, the All-Share Index (ASI) increased by 15.48 percent to 38,243.19 at end-December 2017 from 33,117.48 at end- June 2017, and by 42.30 per cent year-on-year.

The outlook is that the economy is projected to remain on a growth path into the first half of 2018, supported by positive developments in the oil sector and other government initiatives. The near term risks to this outlook, however, remain the delay in the passage and implementation of the FGN 2018 budget, slow credit growth and poor transmission of monetary policy impulses to the real economy, which could undermine output in addition to the perennial challenge of infrastructure deficit. Also, the short to medium-term outlook for price development indicate that inflation would continue to moderate. The key risks to inflation, however, would include: the implementation of the proposed expansionary 2018 Federal Government budget and election-related spending in preparation of the 2019 general elections in the country, high energy costs and continued poor power supply, increased cost of transportation and the disruptive effects of the clashes between farmers and herdsmen, which are likely to feed into higher domestic prices. Nevertheless, monetary policy would remain proactive to minimize the threats to the achievement of the objective of price stability conducive to sustainable economic growth.

GODWIN I. EMEFIELE
Governor, Central Bank of Nigeria

CHAPTER ONE

1.0 OVERVIEW

Monetary policy in the second half of 2017 was shaped by a number of developments in the global and domestic economic and financial environments. On the global front, the key issues were: the continued slow pace of recovery in global oil and other commodity prices, the damage to infrastructure caused by hurricanes - Harvey, Irma and Maria, the reduction in China's uptake of global commodities and financial market uncertainties due to monetary policy normalization in the US. Others included: trade protectionism and immigration challenges, complexities arising from the BREXIT negotiations, continued tensions on the Korean Peninsula as well as geo-political risks associated with the growing right-wing political movements in Europe.

On the domestic front, the stability in the foreign exchange market, arising from measures to manage the demand pressure including the introduction of the Investors' and Exporters' window, and the sustained tight monetary policy stance of the Bank, further contributed to the decline in inflation witnessed during the period. As a result, headline inflation declined progressively from 16.05 per cent in July to 15.37 per cent in December 2017. The food component remained the key driver of headline inflation in terms of its weight in the consumer basket.

The domestic economic environment further improved due largely to rising public and private consumption as a result of higher oil receipts, fiscal stability arising from the implementation of the Economic Recovery and Growth Plan (ERGP), and stability of the exchange rate as well as increased tempo of activities in the key sectors of the economy. These developments along with increased oil production following stability in the Niger Delta region, resulted in domestic output recovery. Accordingly, data from the National Bureau of Statistics (NBS) showed that real GDP in the fourth quarter of 2017 strengthened further by 1.92 per cent from the growth of 1.40 per cent in the preceding quarter of 2017, in contrast to the contraction of 1.73 per cent in the corresponding quarter of 2016. The improved performance was attributed to the growth of both the oil and non-oil sectors. The oil sector grew by 8.38 per cent in the fourth quarter, representing a 26.08 percentage points increase over the contraction of 17.70 per cent in the corresponding quarter of 2016. The non-oil sector also grew remarkably by 1.45 per cent in the fourth quarter in contrast to the contractions of 0.76 and 0.33 per cent in the preceding quarter and the corresponding period of 2016, respectively. The fourth quarter non-oil GDP growth was largely driven by Agriculture (4.23%), Construction (4.14%) and Trade (2.07%). The Services and Industry sectors, however, contracted by 0.55 and 0.03 per cent, respectively. Thus, the growth of the oil sector seems to be spilling over to recoveries in some non-oil activities. Overall, the economy grew by 0.83 per cent in 2017 reversing the contraction of 1.58 per cent in 2016.

Activities in Nigeria's financial markets were influenced by a number of developments in the global economic environment. On the global scene, although the financial markets remained moderately calm, it was under threat from uncertainties around NAFTA renegotiations, BREXIT discussions, and the growing share of companies with low investment grade ratings in the advanced economy bond markets. Other challenges included rising asset valuations and higher leverage arising from continued monetary accommodation, spill-over of financial stability risks to the non-bank and market sectors as well as geo-political tensions on the Korean peninsula and the Middle East. Nevertheless, most currencies appreciated against the US dollar, as oil and other commodity prices continued to improve and earlier expectations of an expansionary US fiscal policy diminished.

The Bank continued to intervene in the foreign exchange market in order to sustain the stability so far achieved and strengthen the gains recorded in the Investors' and Exporters' foreign exchange window. Additional reforms and interventions during the period were aimed at encouraging capital inflows to improve liquidity in the market. These measures were the intensification of the policy on repatriation of export proceeds as well as return of unutilized foreign exchange sourced from CBN auctions. The Bank also sustained the implementation of existing measures including the restriction of access to foreign exchange for 41 items, the use of Bank Verification Number (BVN) in BDC transactions, resumption of sale of foreign exchange by the Bank and International Money Transfer Operators (IMTOs) to BDCs, as well as special foreign exchange auction to targeted sectors and foreign exchange sales for small scale importation. As a consequence, the rates at the bureau-de-change (BDC) and Nigeria Autonomous Foreign Exchange (NAFEX) segments moved towards convergence as demand pressure in the market moderated. In addition, the average naira exchange rate at the inter-bank segment of the foreign exchange market remained stable in the second half of 2017.

The Bank continued to employ various policy instruments in its tool kit in the review period in order to achieve the objective of price and macroeconomic stability. The instruments deployed were: the Monetary Policy Rate (MPR), Cash Reserve Ratio (CRR), Liquidity Ratio (LR), Open Market Operations (OMO), and Discount Window Operations, complemented by interventions in the foreign exchange market. The MPR was maintained at 14.0 per cent throughout the period along with the asymmetric corridor of +200 and -500 basis points around the MPR. The Bank increased its reliance on Open Market Operations (OMO) as the main tool for managing banking system liquidity in the second half of 2017. As a result, total OMO sales rose significantly by 92.87 per cent to ₦7,472.21 billion in the second half from ₦3,874.27 billion in the first half of 2017. The increase in OMO sales in the second half of 2017 was to reduce the level of liquidity in the banking system in order to moderate inflationary pressure, in line with the prevailing non-accommodative monetary policy stance of the Bank. The monetary aggregates performed better than in the first half even though most of the aggregates did not meet their targets for end-December 2017. The development was due to the significant decline in net domestic assets (NDA), following the contraction in credit to government which was, however, moderated by the increase in net foreign assets (NFA) during the review period.

Liquidity conditions in the banking system continued to influence activities in the money market. Money market rates fluctuated upwards in response to the Bank's interventions in the foreign exchange market to stabilize the exchange rate, coupled with increased OMO auctions. These were, however, moderated by the liquidity impact of Federation Account Allocation Committee (FAAC) disbursements, release of balance of Paris Club debt refunds, FGN capital releases, Joint Venture Cash (JVC) call payments and maturing CBN bills and government securities. As a result, the Interbank and OBB rates remained largely above the upper band of the standing facilities corridor. The Nigerian money market reference rate, the NIBOR, recorded mild fluctuations across all tenors in response to the liquidity condition in the banking system.

Activities in the Nigerian capital market in the second half of 2017 were mainly bullish, reflecting investor positive sentiments attributable to generally improving macroeconomic conditions. The All-Share Index (ASI) increased by 15.48 percent to 38,243.19 at end-December 2017 from 33,117.48 at end-June 2017. It also increased by 42.30 per cent compared with 26,874.62 at end-December 2016. The development was traceable to a number of factors including the growing external reserves, stable exchange rate and moderating inflation, on the back of rising crude oil prices, which helped to boost investor confidence in the economy. Also, the sustained tight monetary policy stance of the Bank improved returns on domestic assets and attracted foreign inflows into the capital market. The continued BREXIT uncertainty and the generally accommodative monetary policy stance in the advanced economies helped to support the flow of foreign capital in search of yields in the emerging markets, including Nigeria.

The bond market segment was dominated by Federal Government of Nigeria (FGN) securities in the second half of 2017. There was also some activity in the Sub-national government and corporate bonds segments, with the latter recording the least share by market volume. The 10-year dollar-denominated bond yields for Nigeria decreased by 33 basis points to 4.47 per cent at end-December 2017, from 4.80 per cent at end-June 2017. When compared with 6.35 per cent at end-December 2016, it decreased by 188 basis points, reflecting improved perception by investors of the country's sovereign risk.

Headline inflation (year-on-year) moderated during the second half of 2017, although still substantially above the Bank's benchmark of 6-9 per cent. The price development, however, remained within the lower double-digit range and is unlikely to harm growth, based on available inflation threshold studies for the economy. Staff estimates indicate that year-on-year headline inflation is expected to continue decelerating to 15.35, 14.45 and 13.25 per cent in January, March and June 2018, respectively, driven by prospects of sustained stability in the foreign exchange market, lower food prices and the sustained tight monetary policy stance of the Bank.

Output growth in the second half of 2017 was positive, following the economy's exit from recession in the second quarter of 2017. According to NBS, real GDP in the fourth quarter of 2017 strengthened further by 1.92 per cent from the growth of 1.40 per cent in the preceding quarter of 2017, in contrast to the contraction of 1.73 per cent in the corresponding quarter of 2016.

The economy is projected to remain on a growth path into the first half of 2018, supported by positive development prospects in the oil sector and other government initiatives conducive to growth. Accordingly, the International Monetary Fund (IMF) forecasts Nigeria's output growth in 2018 at 2.1 per cent up from 0.8 per cent in 2017 (IMF, WEO, January 2018), premised on expected stronger activity and the positive effect of restriction on OPEC oil production. Similarly, the World Bank forecasts Nigeria's growth at 2.5 per cent in 2018 up from 1.0 per cent in 2017, premised on the sustenance of rising oil production and continuing reforms in the foreign exchange market, coupled with improved electricity supply. Furthermore, the Federal Government of Nigeria's 2018 appropriation bill is based on the growth projection of 3.5 per cent. The key risks to the promising outlook, however, remain the delay in the passage and implementation of the FGN 2018 budget, thereby denying the economy needed fiscal stimulus; slow credit growth and poor transmission of monetary policy impulses to the real economy, which could undermine output; and perennial challenge of infrastructural deficit, amongst others. In this regard, the policy challenge facing the economy is sustaining the fragile growth in the face of still high, although moderating inflationary pressure. The Bank would continue to design, implement and monitor appropriate monetary policy to ensure that the downside risks stemming from inflation to growth are reined-in in the near to medium term.

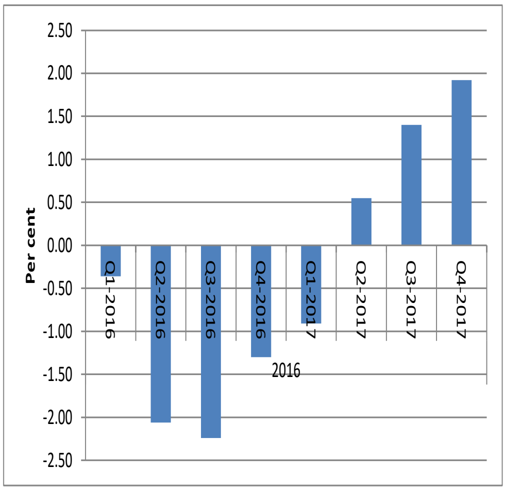
CHAPTER TWO

2.0 OUTPUT IN THE DOMESTIC ECONOMY

In the second half of 2017, the Nigerian economy sustained its recovery, which was however, still fragile. The improvement was largely due to the firming up of crude oil and other commodity prices in the international market and increased oil production owing to sustained peace in the Niger Delta region. Other factors were: the return of policy stability as reflected in the implementation of the Federal Government's Economic Recovery and Growth Plan (ERGP) as well as reforms in the foreign exchange market leading to improved investor confidence in the economy. The risks to this modest recovery, however, remained the emerging problem of delays in budget passage and implementation, weak aggregate demand from the buildup of salary arrears and contractors' debt by government, and disruption of agricultural activities due to farmer-herdsmen conflict as well as energy supply challenges. Policy is expected to focus on these challenges in order to sustain the recovery.

As a result of these developments, real GDP in the third quarter of 2017 grew by 1.40 per cent (year-on-year) up from 0.72 per cent in the preceding quarter in contrast to the contraction of 2.34 per cent in the corresponding period of 2016. The growth was largely attributed to the performance of the oil sector which grew substantially by 25.89 per cent in the third quarter of 2017, representing an increase of 47.90 percentage points compared with the contraction of 22.01 per cent in the corresponding quarter of 2016. The recovery of the oil sector, if sustained, signposts the return of the economy to its growth trajectory. In contrast, non-oil real GDP shrank by 0.76 per cent in the third quarter of 2017, compared with the growth of 0.03 per cent in the corresponding quarter of 2016 and 0.45 per cent in the preceding quarter.

Figure 2.1
Real GDP Growth (%) 2016 Q1 – 2017 Q4



Source: NBS

In the fourth quarter, output growth strengthened further by 1.92 per cent from the growth of 1.40 per cent in the preceding quarter of 2017, in contrast to the contraction of 1.73 per cent in the corresponding quarter of 2016. The improved performance was attributed to the growth of both the oil and non-oil sectors. The oil sector grew by 8.38 per cent in the fourth quarter, representing a 20.76 percentage points increase over the contraction of 12.38 per cent in the corresponding quarter of 2016. The non-oil sector also grew, remarkably, by 1.45 per cent in the fourth quarter in contrast to the contractions of 0.76 and 0.33 per cent in the preceding quarter and the corresponding period of 2016, respectively. The fourth quarter non-oil GDP growth was largely driven by Agriculture (4.23%), Construction (4.14%) and Trade (2.07%). However, Services and Industry sectors contracted by 0.55 and 0.03 per cent, respectively. The growth in the oil sector seems to be spilling over to recoveries in some non-oil activities. Overall, the economy grew by 0.83 per cent in 2017 from a contraction of 1.58 per cent in 2016.

2.1 DOMESTIC ECONOMIC ACTIVITIES

Activities in the oil sector complemented by non-oil sector performance drove the fragile recovery witnessed in the second half of 2017. During the third quarter, the oil sector grew by 25.89 per cent, representing an increase of 47.90 percentage points compared with the contraction of 22.01 per cent in the corresponding quarter of 2016. Oil production in the third quarter was estimated at an average of 2.03 million barrels per day (mbpd), which was 0.15 mbpd higher than the daily average production of 1.87 mbpd recorded in the second quarter of 2017.

The non-oil sector, however, contracted by 0.76 per cent in the third quarter of 2017, reversing the growth of 0.45 and 0.03 per cent recorded in the preceding quarter and the corresponding period of 2016, respectively. The contraction of non-oil sector was due mainly to shrinkage in the Services (2.95%), Industry (2.79%), Trade (1.74%) and Construction (0.46%) sectors, compared with their corresponding growth rates of -1.08, -4.22, -1.38 and -6.13 per cent, respectively. Although the non-oil sector contracted, the agricultural sub-sector grew by 3.06 per cent to support the output recovery.

In the fourth quarter of 2017, both the oil and non-oil sectors contributed to output recovery. The oil sector grew by 8.38 per cent, from a contraction of 17.70 per cent in the corresponding period of 2016. This was, however, a moderation when compared with the growth of 25.89 per cent in the preceding quarter. Accordingly, average daily crude oil production in the fourth quarter fell to 1.91 mbpd from 2.03 mbpd in the preceding quarter. This was, however, higher by 0.15 mbpd compared with 1.76 mbpd in the corresponding period of 2016. The non-oil sector also grew by 1.45 per cent from the contractions of 0.76 and 0.33 per cent in the preceding quarter and the corresponding period of 2016, respectively. The growth in the non-oil sector was mainly due to activities in Transport (16.57%), Utilities (12.99%), Crop Production (4.58%), Fishing (4.05%), Arts, Entertainment & Recreation (3.54%) and Forestry (2.83%). This compares with their respective growth rates of -5.32, -2.27, 4.36, 0.76, 2.04 and 2.22 per cent, in the corresponding period of 2016. The improvement in non-oil sector in the fourth quarter reflected the positive spillover effects and fiscal releases associated with expansion in the oil sector.

Figure 2.2
Non-oil Sector Performance 2016Q1-2017Q4

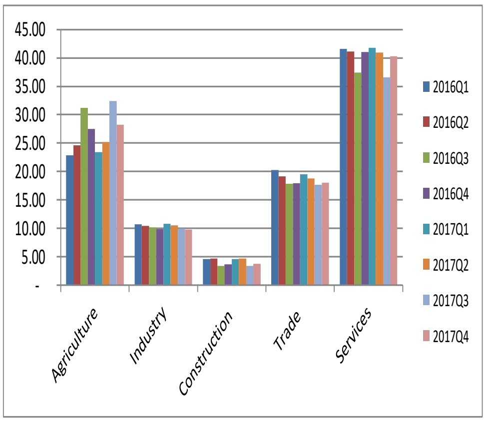
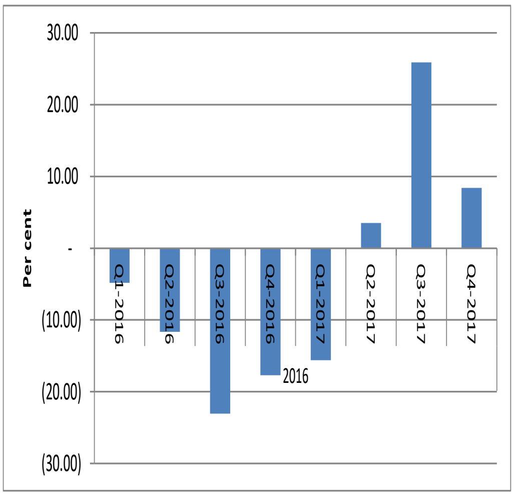


Figure 2.3
Performance of the Oil Sector 2016Q1-2017Q4



Source: NBS

2.2 Sectoral Analysis

This section highlights the sectoral performance of the economy and the key institutional factors that contributed to domestic output in the review period.

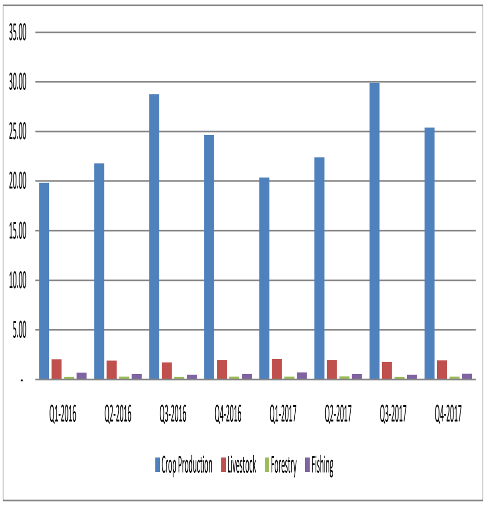
2.2.1 Agriculture

Real agricultural GDP grew by 3.06 per cent in the third quarter of 2017, up from 3.01 per cent in the preceding quarter but lower than 4.54 per cent in the corresponding period of 2016. Activities in the agricultural sector were mainly driven by the performance of Forestry (3.95%), crop production (3.19%) and livestock (2.52%), which compares with their respective growth rates of 2.08, 4.88 and 0.76 per cent, in the corresponding quarter of 2016. Fishing, however, contracted by 2.84 per cent, below the contraction 0.34 per cent in the corresponding period of 2016.

During the third quarter, the contribution of the sector to real GDP stood at 29.15 per cent, representing a decline of 2.06 percentage points compared with 31.21 per cent in the corresponding period of 2016.

In the fourth quarter of 2017, output of the agricultural sector grew by 4.23 per cent, up from 3.06 per cent in the preceding quarter. This represented a 0.20 percentage point increase over the growth of 4.03 per cent in the corresponding quarter of 2016. At 4.58 per cent, Crop Production was the main driver of agricultural output growth in the quarter, followed by Fishing (4.05%), Forestry (2.83%) and Livestock (0.19%). This compares with their respective growth rates of 4.36, 0.76, 2.22 and 1.23 per cent in the corresponding quarter of 2016. The share of agriculture in total output at 26.18 per cent in the fourth quarter of 2017 was below the 27.45 per cent recorded in the corresponding period of 2016.

Figure 2.4
Agricultural Sector Contribution by Activity, 2016Q1-2017Q4



Source: NBS

2.2.1.2 Agricultural Policies and Institutional Support

During the second half of 2017, the performance of agricultural sector benefited from a number of policies, reforms and institutional support, which included:

The Agricultural Credit Guarantee Scheme (ACGS)

In the second half of 2017, the scheme guaranteed a total of 20,268 loans valued at ₦2.822 billion for three commercial banks and some microfinance banks, compared with 21,073 loans valued at ₦3.03 billion for two commercial and 36 microfinance banks in the first half of 2017. This represented a decrease of 3.82 per cent and 6.86 per cent in the number and value of loans guaranteed, respectively. During the same period, ₦3.01 billion was repaid by 22,475 projects compared with ₦2.94 billion from 18,600 projects in the corresponding period of 2016. This performance reflected an increase of 2.3 and 20.83 per cent in the value and number of loans repaid, respectively.

The N200 Billion Commercial Agriculture Credit Scheme (CACS)

The sum of ₦80.96 billion was disbursed to 11 banks for 34 projects under the Scheme in the second half of 2017, compared with ₦79.56 billion disbursed to 11 banks for 23 projects in the preceding period. This represented an increase of 1.76 and 47.83 per cent in the value and number of projects financed, respectively, under the Scheme. Total repayments in the second half of 2017 stood at ₦28.825 billion for 191 projects.

N220 Billion Micro, Small and Medium Enterprises Development Fund (MSMEDF)

During the review period, the following activities were carried out under the Scheme:

- **Disbursements to SME and Micro Enterprises**

The sum of ₦1.59 billion was disbursed in the second half of 2017 compared with ₦1.59 billion in the first half of 2017.

- **Anchor Borrowers' Programme (ABP)**

In the second half of 2017, the sum of ₦13.406 billion was disbursed to 73,279 farmers in 18 states.

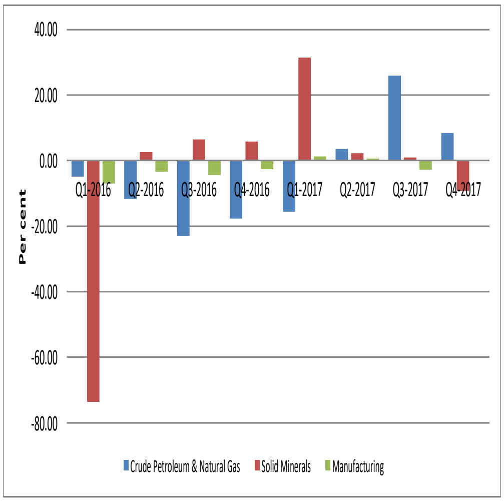
2.2.2 Industry

2.2.2.1 Industrial Production

Industrial output growth strengthened by 10.51 per cent in the third quarter of 2017, up from 2.04 per cent in the preceding quarter, in contrast to the 13.98 per cent contraction in the corresponding period of 2016. The main drivers of this outcome were activities in the Crude petroleum & natural gas, and Solid minerals sub-sectors, which grew by 25.89 and 0.92 per cent, respectively, while Manufacturing contracted by 2.85 per cent. This performance compares reasonably with their respective growth rates of 3.53, and 2.28 per cent in the preceding quarter. When compared with the corresponding period of 2016, the Solid mineral sub-sector grew by 6.52 per cent, while crude petroleum & natural gas contracted by 22.01 per cent. The modest growth of the solid mineral sub-sector was attributed to activities in Metal Ores (10.70%), and Quarrying & Other Mining (1.86%). The contraction in the Manufacturing sub-sector was largely driven by shrinkage in Oil Refining (45.41%), Motor Vehicle & Assembly (21.26%), and Cement (4.56%). This compares with their respective growth rates of -0.86, -33.31 and-6.26 per cent in the corresponding period of 2016.

Industrial sector growth, however, moderated to 3.53 per cent in the fourth quarter of 2017, from 10.51 per cent in the preceding quarter. When compared with the contraction of 9.52 per cent recorded in the corresponding period of 2016, the industrial sector grew by 13.05 percentage points. The moderation in Industrial output was traceable to the 9.18 per cent contraction in the solid minerals sub-sector, in contrast to the growth of 8.38 and 0.14 per cent in Crude petroleum & natural gas and Manufacturing sub-sectors, respectively. This compares with their respective growth rates of 5.76, 17.70 and 2.54 per cent in the corresponding quarter. The shrinkage of the Solid Minerals sub-sector which dampened the Industrial performance during the period was largely due to the 10.94 per cent contraction in Quarrying and Other Mining activity. Consequently, the share of Industry in the total GDP declined from 19.01 per cent in the third quarter to 16.20 per cent in the fourth quarter of 2017.

Figure 2.5
Industrial Sector's Contribution by Activity, 2016Q1-2017Q4



2.2.2.2 Industrial Policy and Institutional Support

The Industrial sector benefited from the continuation of a number of reforms, policies and incentives in the review period. These include:

The N300 Billion Power and Airline Intervention Fund (PAIF)

During the review period, ₦1.98 billion was disbursed to two power projects - Azura Power (₦1.699billion), and Kano Hydro Power Project (₦0.28billion). Also, ₦13.721billion was repaid by 38 obligors.

The N213 Billion Nigeria Electricity Market Stabilization Facility (NEMSF)

The Facility released ₦5.465billion to 3 market participants (Eko Disco, Egbin Power, and Pan Ocean) in the review period. In addition, ₦2.511billion was repaid by 8 obligors.

Real Sector Support Facility (RSSF)

In the second half of 2017, ₦22.43 billion was disbursed to eleven (11) projects under the Facility compared with ₦22.73 billion disbursed to seven projects in the first half. This represented a decrease of 1.3 per cent.

Entrepreneurship Development Centres (EDCs)

A total of 7,859 participants were trained in the Entrepreneurship Development Centres (EDCs) in the second half of 2017, comprising 4,113 (52.33%), females and 3,746 (47.67%), males.

Youth Entrepreneurship Development Programme (YEDP)

In the review period, ₦126.98 million was disbursed to 3 entrepreneurs under the Youth Entrepreneurship Development Programme (YEDP).

Nigeria Bulk Electricity Trading – Payment Assurance Facility (NBET-PAF)

In order to address the protracted liquidity problem facing power generation and distribution companies, the Federal Executive Council approved a payment assurance guarantee of ₦701 billion for the power sector. The fund is to be provided by the Central Bank of Nigeria under "Nigeria Bulk Electricity Trading – Payment Assurance Facility (NBET-PAF)". The facility is to provide bridging finance that will enable NBET provide minimum level of payment to generation companies. The payment will in turn allow the generation companies to meet their obligations to gas suppliers, and thus increase the level of power generation in the country. The NBET-Payment Assurance Facility was a directive of the Federal Executive Council (FEC), and was backed by a Federal Ministry of Finance Guarantee for the payment of Interest and Principal as they fall due, where NBET is unable to pay from appropriation.

The terms and condition of the loan include: borrower - Nigeria Bulk Electricity (NBET) Trading Plc; interest rate - 5% per cent per annum; loan tenor - ten (10) years, not exceeding December 31, 2028; moratorium - Two (2) years after Effective Date; interest payment shall commence from January 2018, while principal repayment shall commence from January 2019. Also, a letter of Commitment by NBET to provide for the repayment obligation in its annual budget for appropriation each year until the loan is fully repaid, to be endorsed by the Federal Ministry of Finance (FMoF) and the Ministry of Budget and National Planning. Guarantee from the Federal Ministry of Finance (FMoF) to make payment as scheduled should there be non-release from the budgetary allocation was also required.

Under the funding arrangement, CBN was to subscribe to debenture to be issued by NESI Stabilization Strategy Limited (NESI SS Ltd), and set up an NBET-Payment Assurance Facility under NESI SS Ltd using the structure under the Nigeria Electricity market Stabilization Facility (NEMSF).

Drawdowns will be made on a monthly basis based on invoices, over a period which shall not exceed 24 months. The applications for disbursement will contain comprehensive breakdowns of the elements of the payment showing the amounts due to each participating generator and its approved third parties. CBN will review NBET's submission and credit the beneficiaries that meet full disbursement criteria. Applications for disbursement will be sent by NBET and confirmed by the Honorable Minister, Federal Ministry of Power.

So far, the sum of ₦109.689billion had been paid to the generating and gas companies for invoices for March to July, 2017 as directed by NBET the primary obligor.

The facility has restored the confidence of gas suppliers in the electricity market. Also, the effort of the CBN to stabilize the electricity market in Nigeria could mitigate the risk of high non-performing loans in the banking sector due to the huge debt owed by the power industry to gas suppliers and the generating companies.

2.2.3 Construction

In the third quarter of 2017, the contraction in the construction sector moderated to 0.46 per cent compared with the contraction of 6.13 per cent in the corresponding quarter of 2016. In the preceding quarter, the sector, however, grew marginally by 0.13 per cent.

During the fourth quarter, the sector grew by 4.14 per cent in contrast to the contractions of 6.03 and 0.46 per cent in the corresponding period of 2016 and the preceding quarter of 2017. The share of Construction in the total GDP improved from 3.04 per cent in the third quarter to 3.50 per cent in the fourth quarter of 2017. The lackluster performance of the sector may not be unconnected with the poor appropriation and implementation of capital budgets in the country.

2.2.4 Trade

The contraction of the trade sector intensified to 1.74 per cent in the third quarter of 2017 from contractions of 1.38 and 1.62 per cent in the corresponding period of 2016 and preceding quarter, respectively.

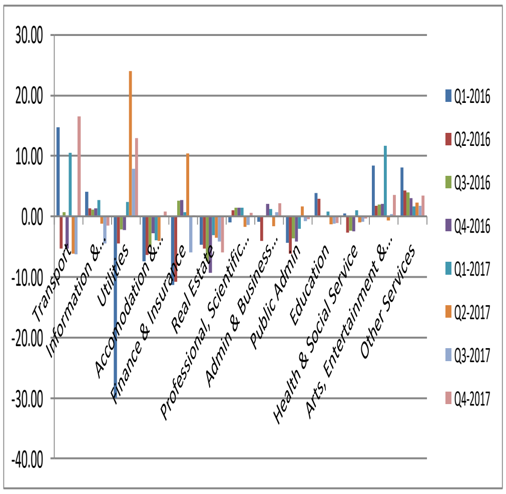
During the fourth quarter, however, activity in the trade sector recovered, as the sector grew by 2.07 per cent from the contractions of 1.44 and 1.74 per cent in the corresponding period of 2016 and preceding quarter of 2017, respectively. The recovery of trade activities was traceable to reforms in the foreign exchange market, particularly the establishment of Investors' and Exporters' Window, which enhanced access to foreign exchange by eligible investors. The share of Trade in the total GDP improved from 15.90 per cent in the third quarter to 16.75 per cent in the fourth quarter of 2017.

2.2.3 Services Sector

The Services sector contracted during the second half of 2017 as in the first half of the year. In the third quarter, the contraction of the sector was more severe at 2.95 per cent compared with the contractions of 1.08 and 0.15 per cent in the corresponding period of 2016 and preceding quarter of 2017. The contraction of the sector was driven by shrinkages of 6.25, 5.96, 4.48, 4.12, 1.38 and 1.22 per cent in Transport, Finance & Insurance, Information & Communication, Real Estate, Professional, Scientific & Technical Service and Education sub-sectors. The contraction of the sector was, however, moderated by the growth of 7.84, 1.72, and 0.68 per cent in utilities, other services and administrative & support services sub-sectors, respectively.

During the fourth quarter, the contraction in the Services sector moderated by 0.55 per cent from 1.56 and 2.95 per cent in the corresponding period of 2016 and the preceding quarter of 2017, respectively. The moderation was attributed mainly to the growth of 16.57, 12.99, 3.54, 3.46 and 2.16 per cent in Transport, Utilities, Arts, Entertainment & Recreation, Other Services, and Administrative & Support Services. The moderation was, however, softened by the continued contractions of the following sub-sectors: Real Estate (-5.92%), Information and Communication (-1.46%) and Education (-1.04%). The effect of weak aggregate demand appears to be reflected more sharply in the performance of the sector which has remained in recession since the second quarter of 2016. The continued contraction of the Services Sector moderated its contribution to GDP from 38.31 per cent in the corresponding period of 2016 to 37.38 per cent in the fourth quarter of 2017.

Figure 2.6
Services Sub-Sector Contribution, 2016Q1-2017Q4



2.2.6 The Oil Sector

The performance of the oil sector improved significantly during the review period. As a result, average crude oil production rose to 2.03 million barrels per day (mbpd) in the third quarter of 2017, from 1.61 mbpd and 1.87 mbpd in the corresponding period of 2016 and the preceding quarter of 2017, respectively. In the fourth quarter, average daily crude oil production, however, moderated slightly to 1.91 mbpd from 2.03 mbpd in the preceding quarter. This was, however, higher by 0.15 mbpd when compared with 1.76 mbpd in the corresponding period of 2016.

During the review period, crude oil prices rose due mainly to developments in the global economy. These were the agreement between OPEC and some non-OPEC producers to cap production as well as economic recovery in some advanced and emerging markets and developing economies. Thus, the price of Nigeria's reference crude, the Bonny Light 37^{0}API, rose steadily from US$49.01 per barrel in July to US$51.67pb in September and peaked at US$60.42pb in December, 2017. Overall, the average price of Bonny Light of US$54.91pb in 2017 was US$10.41pb above the Federal Government of Nigeria's 2017 budget benchmark of US$44.50pb.

Figure 2.7
Quarter Oil Production (2016Q1-2017Q4)

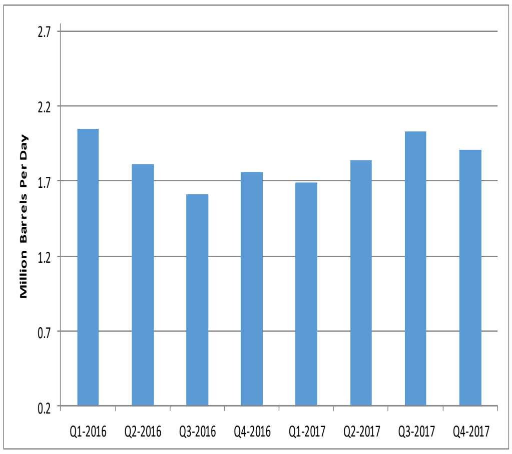
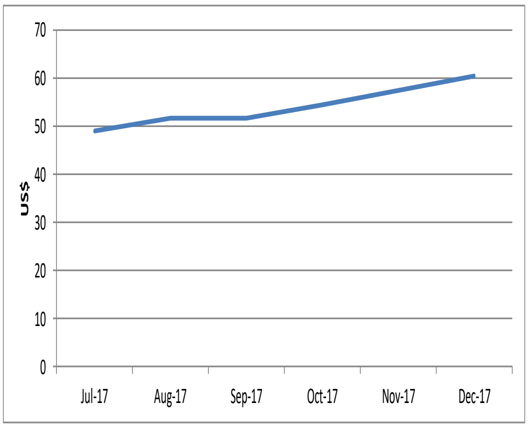


Figure 2.8
Monthly Bonny Light Price, July – December 2017



Natural Resources Scarcity and Conflicts in Nigeria.

Natural resources including land, water, forests, and other components of the ecosystem are available only in limited quantity. Climatic changes and human activities including population explosion interact to further make these natural resources scarcer. In most developing countries including Nigeria, the situation is worsened by the lack of social and technical capital to maximise the use of these resources. Studies have shown that the more people are dependent on sensitive forms of natural capital, and rely less on economic and or social forms of capital, the more at risk they are from climate changes and prone to conflict when such resources are threatened. This is because the depletion of the natural capital forces competition over marginal resource field and in some cases migration from resource-depleted areas to areas adjudged to have more resources. Such movements generate tension, threats, when not proactively addressed, result in conflicts. In the African savannah belt, for example, increased agricultural activity continue to exert pressure on the land, reducing soil fertility and forcing farmers to shift to previously nucleated land. In an environment where you also have pastoralists who traditionally treat uncultivated land as common resource, this practice is bound to lead to conflict.

Resource use conflict is generally viewed as a situation of individuals or groups competing for exclusive access to the use or ownership of limited resources. Conflicts often arise because people have different uses and interests or rights in the resources such as water, forest, pastures and land, or want to use them in different ways. In the process of pursuing their different interests, disagreements arise when the priorities of one group do not accommodate those of other(s). In recent years, the scope and magnitude of natural resource conflicts have increased and intensified. In some areas, they have become violent resulting in loss of lives and properties, further plunging individuals and communities into extreme poverty and deprivation. Today it is common to find settlements of Internally Displaced Persons (IDP) camps housing thousands of people who have been dislocated from their original homes by violent conflicts.

In view of the foregoing, the farmers-herders conflict in Nigeria can be analysed as the outcome of four key drivers: limited supply of natural resources, population growth and increasing demand for natural resource, climate change and its impact on the supply of natural resources, and absence of proper institutional arrangements and technical capital to facilitate the efficient management of natural resources.

Although nature is generous, its provision of material resources is limited. The earth surface is made up of land and water with the latter accounting for more than 70 per cent of the earth total area. Similarly, while the size of the total surface area has remained unchanged, same cannot be said of the ratio between land and water surface areas in view of climate change effects over time. More obvious, however, is the population explosion over this surface in the last millennium and the necessity for continued access to natural resources for its survival.

Environmental scarcity constrains economic development and contributes to migrations, situations which sharpens existing distinction among social groups, weakens states and in turn make them vulnerable to conflicts and insurgencies. One of the earliest contributors of the discussion on resources scarcity and violent conflict is Thomas Malthus (1798). In his *Essay on the Principle of Population*, Malthus posited that the human population grows exponentially while the supply of food grows only in an arithmetic ratio such that over time, these expansion rates would inevitably lead to crises. Thus Malthusianism agrees that there is scarcity of natural resources that acts as constraints on human behaviour, and that there are linkages between this and violent conflict.

Nigeria has remained largely an agricultural society depending on the available 77 per cent (as at 2015) of its total land area for agricultural activities. The country's population has grown from a little above 50 million in the 60s to around 180 million today. The country's human activities and the livelihood of its population have continued to revolve around nature-dependent agriculture. This explains why most communal/group conflicts have continued to be land-related as parties desire to have unfettered access to the available land for their survival. In the case of relationship between farmers and herders, farmers would want to secure their cultivated land areas and practice shifting cultivation under rain-fed agriculture; the practice overtime, however, reduces the space for open grazing. Thus, for herders who have often seen uncultivated land as a common resource over which they can graze their cattle, the narrowing of the space and the increasing likelihood of the herds straying into cultivated lands makes the relationship between the groups conflict-prone.

Societies in the western world are today free of natural resource-induced conflicts having developed and applied social and technical capital in the use of their natural resources. In Nigeria, as in the rest of most developing societies, the absence of social reorganization, development of indigenous technical-know-how or its adaptation and effective institutions to guide and enforce contractual relationship between individuals or groups have led to growing conflicts among groups as exemplified by border-communities crisis and the farmers-herders conflicts.

To address this ugly development that is now assuming a dangerous dimension in Nigeria, the state must quickly put in place measures to de-escalate violence in communities already affected and remain proactive in forestalling further occurrence. The state must lead in reorienting the citizenry on the limited availability of natural resources, institute a process of social reorganization through effective institutional arrangements, and support the development of technical capital and know-how in the exploitation of environmental resources. The Africa Green Belt project is one important initiative that must be followed through with every commitment by the Federal Ministry of Environment. The project involves the building a forest vegetation shelter across the West African Sahel belt that passes through Sokoto, Katsina, Kano, Yobe and Borno States. There is need for a deliberate effort to commit sufficient resources by the government for the implementation of this clearly beneficial project for the country. Overall, acknowledging conflict as a common feature of any resource dependent/use system is a prerequisite for developing a framework for its sustainable solution.

CHAPTER THREE

3.0 PRICE DEVELOPMENTS

The inflationary pressure in the domestic economy continued to abate in the second half of 2017, largely reflecting the sustained tight monetary policy stance of the Bank. All measures of inflation maintained a downward trajectory throughout the review period, although, headline inflation still remained outside the Bank's target range of 6 - 9 per cent. These domestic price developments broadly mirrored both supply and demand side factors.

On the supply side, the pressure in the foreign exchange market moderated, with pass-through to lower domestic prices in the review period. Accordingly, the naira exchange rate appreciated in all segments of the market following recent reforms and interventions by the Bank. These included the introduction of a number of measures to encourage capital inflow and improve liquidity in the foreign exchange market. These measures were the intensification of the policy on repatriation of export proceeds as well as return of unutilized foreign exchange sourced from foreign exchange auctions to the CBN. The Bank also sustained the implementation of existing measures including the newly introduced Investors' & Exporters' window, restriction of access to foreign exchange for 41 items, the use of Bank Verification Number (BVN) in BDC transactions, and resumption of sale of foreign exchange to BDCs by the Bank and International Money Transfer Operators (IMTOs). In addition, the improved accretion to external reserves following the recovery of crude oil prices supported the appreciation of the naira.

On the demand-side, price developments reflected activities in the money market, which was tight towards the end of the review period. The Inter-Bank Call and Open Buy Back (OBB) rates continued to fluctuate on account of changing liquidity conditions in the banking system. Periods of excess liquidity largely reflected maturing securities, disbursement of the second tranche of the Paris Club refunds to sub-national governments, and the cautious approach to lending by DMBs. Overall, the sustained Open Market Operations (OMO) helped to tighten market liquidity and rein-in inflation.

3.1 Trends in Inflation

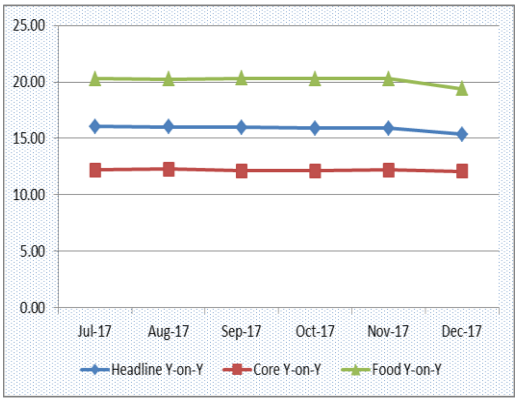
All measures of inflation (headline, core and food), maintained a downward trend in the review period. The headline, core and food measures of the consumer price index (CPI) stood at 237.0, 225.2 and 250.0 in July 2017 compared with 246.4, 233.8 and 261.0, respectively, in December 2017. Accordingly, food inflation (year-on-year) declined by 0.86 percentage point from 20.28 per cent in July to 19.42 per cent in December 2017. Similarly, core inflation declined by 0.10 percentage point from 12.20 per cent in July to 12.10 per cent in December 2017. As a result, headline inflation declined by 0.58 percentage point from 16.05 per cent in July to 15.37 per cent in December 2017 (Figure 3.1 and Table 3.1). Thus, food inflation was the major driver of overall moderation in consumer prices during the period, although the core measure also contributed (Table 3.4).

Table 3.1
Inflation Rates, July – December 2017

	Headline Inflation			Core Inflation			Food Inflation		
	CPI	Y-on-Y	12MMA	CPI	Y-on-Y	12MMA	CPI	Y-on-Y	12MMA
2017-Jul	237.00	16.05	17.47	225.20	12.20	15.60	250.00	20.28	18.25
2017-Aug	239.30	16.01	17.33	227.30	12.30	15.37	252.90	20.25	18.57
2017-Sep	241.20	15.98	17.17	229.10	12.10	14.90	255.10	20.32	18.88
2017-Oct	243.00	15.91	16.97	230.90	12.10	14.41	257.20	20.31	19.14
2017-Nov	244.90	15.90	16.76	232.60	12.20	13.93	259.50	20.31	19.39
2017-Dec	246.40	15.37	16.50	233.80	12.10	13.46	261.00	19.42	19.55

Source: *Nigerian National Bureau of Statistics data base*

Figure 3.1
Headline, Core and Food Inflation Rates (July – December 2017)



Source: *Nigerian National Bureau of Statistics data base*

3.1.1 Headline Inflation

The decrease in major components of headline inflation continued during the second half of the year as reflected in the downward trend in domestic prices. Food and Non-Alcoholic Beverages remained the major driver of the decline in headline inflation, falling from 10.60 per cent in July to 10.22 per cent in December, 2017. This was followed by housing, water, electricity, gas and other fuels, which decreased slightly from 1.78 per cent to 1.53 per cent over the same period (Table 3.2 and Figure 3.4). Overall, headline inflation fell significantly, due to the combined effects of decreases in the prices of food & non-alcoholic beverages; housing, water, electricity, gas & other fuels; as well as reduction in imported products.

The stability in the foreign exchange market, arising from measures to manage the demand pressure including the introduction of the Investors' and Exporters' window, further contributed to the decline in inflation witnessed during the period. Other contributory factors were the sustained tight monetary policy stance of the Bank and fiscal stability following the implementation of the Federal Government's Economic Recovery and Growth Plan (ERGP).

On a month-on-month basis, headline inflation declined from 1.21 per cent in July to 0.59 per cent in December, 2017. The major components that accounted for the decline were the prices of food and non-alcoholic beverages, which fluctuated downwards from 0.82 per cent in July to 0.32 per cent in December; and clothing and footwear, from 0.09 per cent in July to 0.05 per cent in December, 2017 (Table 3.3 and Figure 3.5).

Table 3.2
Major Components of Headline Inflation (Y-on-Y), July-December 2017

	Headline	Food & Non-Alcoholic Bev.	Clothing & footwear	Housing, Water, Elect.Gas & Other Fuel	Furnishings, Household Equip &HH Maint.	Health	Transport	Education
Jul-17	**16.05**	10.6	1.17	1.78	0.56	0.27	0.75	0.53
Aug-17	**16.01**	10.61	1.18	1.7	0.59	0.29	0.75	0.49
Sep-17	**15.98**	10.65	1.18	1.63	0.6	0.29	0.76	0.45
Oct-17	**15.91**	10.65	1.17	1.58	0.61	0.29	0.77	0.42
Nov-17	**15.9**	10.66	1.15	1.56	0.62	0.3	0.78	0.41
Dec-17	**15.37**	10.22	1.12	1.53	0.61	0.3	0.78	0.4
Change btw Jul & Dec. 2017	**-0.68**	-0.38	-0.05	-0.25	0.05	0.03	0.03	-0.13

Figure 3.2
Major Components of Headline Inflation (Y-on-Y), July-December 2017

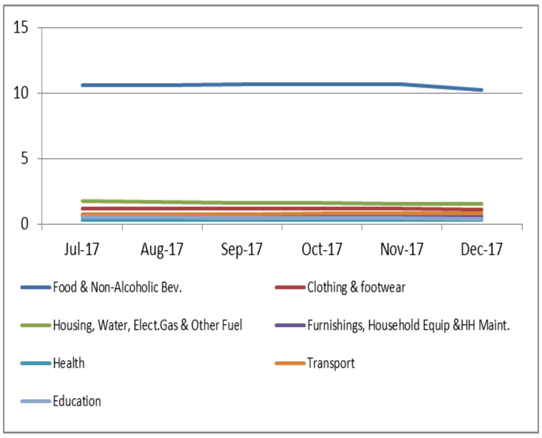
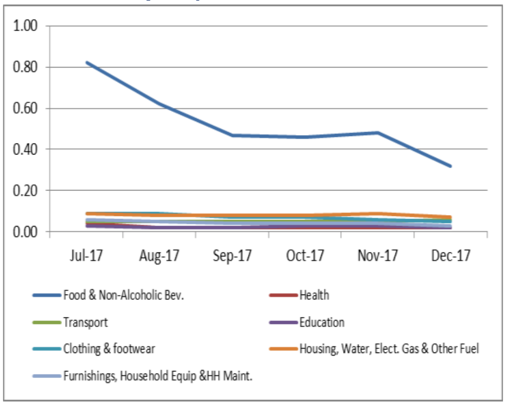


Table 3.3
Major Components of Headline Inflation (M-on-M), July-December 2017

	Headline	Food & Non-Alcoholic Bev.	Health	Transport	Education	Clothing & footwear	Housing, Water, Elect. Gas & Other	Furnishings, Household Equip &HH Maint.
Jul-17	**1.21**	0.82	0.04	0.05	0.03	0.09	0.09	0.06
Aug-17	**0.97**	0.62	0.02	0.05	0.02	0.09	0.08	0.05
Sep-17	**0.78**	0.47	0.02	0.05	0.02	0.07	0.08	0.04
Oct-17	**0.76**	0.46	0.02	0.05	0.03	0.07	0.08	0.04
Nov-17	**0.78**	0.48	0.02	0.05	0.03	0.06	0.09	0.04
Dec-17	**0.59**	0.32	0.02	0.06	0.02	0.05	0.07	0.03
Change btw July & Dec. 2017	-0.62	-0.5	-0.02	0.01	-0.01	-0.04	-0.02	-0.03

Figure 3.3
Major Components of Headline Inflation (M-on-M), July-December 2017



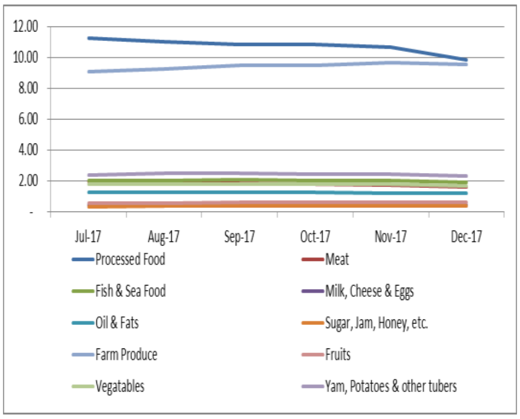
3.1.2 Food Inflation

Food inflation (year-on-year) fluctuated downwards from 20.32 per cent in July to 19.42 per cent in December 2017, a decrease of 0.90 percentage point. The major source of the decrease was the price of processed food which fell by 1.36 percentage points from 11.22 to 9.86 per cent. Farm produce, however, rose by 0.50 percentage point from 9.06 per cent in July to 9.56 per cent in December 2017. The decrease in the price of processed food was accounted for by the fall in the prices of meat, fish and sea food, and oil & fat by 0.36, 0.08 and 0.05 percentage point, respectively. The policy drivers of the fall in processed food were largely the favourable pass-through of lower prices to imported food on account of stability in the foreign exchange market during the period. Other complimentary factor was the sustained tight monetary policy stance of the Bank.

Table 3.4
Major Components of Food Inflation (Y-on-Y), July- Dec 2017

	FOOD	Processed Food	Meat	Fish & Sea Food	Milk, Cheese & Eggs	Oil & Fats	Sugar, Jam, Honey, etc.	Farm Produce	Fruits	Vegatables	Yam, Potatoes & other tubers
Jul-17	**20.28**	11.22	1.95	2.00	0.43	1.22	0.33	9.06	0.54	1.80	2.36
Aug-17	**20.25**	11.02	1.88	2.02	0.44	1.24	0.35	9.23	0.56	1.80	2.45
Sep-17	**20.32**	10.82	1.85	2.04	0.44	1.25	0.36	9.50	0.57	1.80	2.47
Oct-17	**20.31**	10.83	1.78	2.03	0.45	1.23	0.36	9.47	0.58	1.78	2.44
Nov-17	**20.31**	10.66	1.72	2.01	0.45	1.21	0.37	9.65	0.59	1.76	2.42
Dec-17	**19.42**	9.86	1.59	1.92	0.44	1.17	0.36	9.56	0.57	1.68	2.33
Change btw July & Dec. 2017	-0.86	(1.36)	(0.36)	(0.08)			(0.36)	0.50		(0.12)	(0.03)

Figure 3.4
Major Components of Food Inflation (Y-on-Y), Jul - Dec 2017

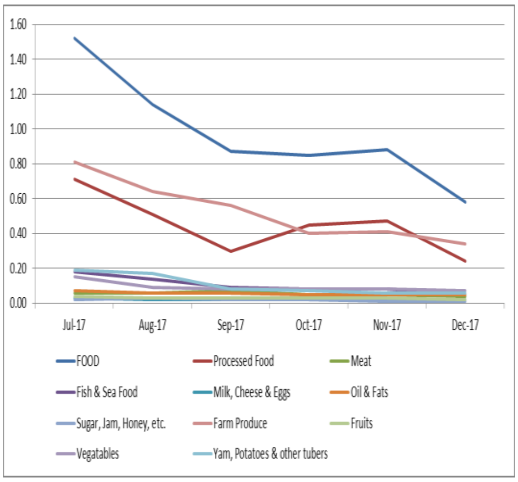


In line with the year-on-year trend, food inflation in general, fell on a month-on-month basis. It fluctuated downwards by 0.94 percentage point from 1.52 per cent in July to 0.58 per cent in December 2017. The price of processed food fell by 0.47 percentage point from 0.71 per cent in July 2017 to 0.24 per cent in December 2017. Similarly, the price of farm produce declined by 0.47 percentage point from 0.81 per cent to 0.34 per cent in the same period. Thus, the 0.94 percentage point decrease in food inflation was equally due to the 0.47 percentage point apiece decrease in processed food and farm produce. The key driver of the decrease in the processed food category was fish and sea food which fell by 0.13 percentage point, while that of farm produce were Yam, Potatoes & Other tubers (-0.13 percentage point) and Vegetables (-0.08 percentage point).

Table 3.5
Major Components of Food Inflation (M-on-M), July December 2017

	FOOD	Processed Food	Meat	Fish & Sea Food	Milk, Cheese & Eggs	Oil & Fats	Sugar, Jam, Honey, etc.	Farm Produce	Fruits	Vegatables	Yam, Potatoes & other tubers
Jul-17	**1.52**	0.71	0.06	0.18	0.03	0.07	0.02	0.81	0.04	0.15	0.19
Aug-17	**1.14**	0.51	0.06	0.14	0.02	0.06	0.03	0.64	0.03	0.09	0.17
Sep-17	**0.87**	0.30	0.07	0.09	0.02	0.06	0.02	0.56	0.03	0.08	0.08
Oct-17	**0.85**	0.45	0.05	0.08	0.02	0.05	0.02	0.40	0.03	0.08	0.07
Nov-17	**0.88**	0.47	0.05	0.08	0.02	0.05	0.01	0.41	0.03	0.08	0.06
Dec-17	**0.58**	0.24	0.04	0.05	0.02	0.05	0.01	0.34	0.02	0.07	0.06
Change btw July & Dec. 2017	**-0.94**	-0.47	-0.02	-0.13			0.00	-0.47		-0.08	-0.13

Figure 3.5
Major Components of Food Inflation (M-on-M), July - Dec 2017



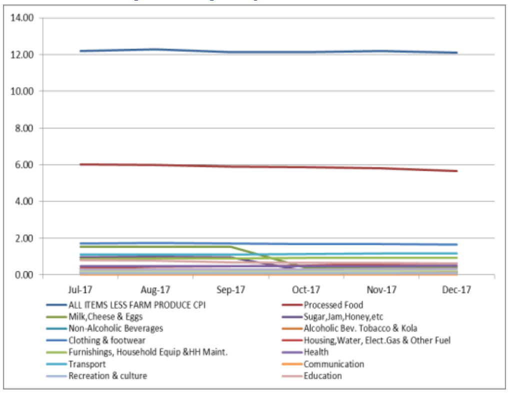
3.1.3 Core Inflation

Core inflation (year-on-year) trended downwards from 12.21 per cent in July 2017 to 12.09 per cent in December 2017, a decrease of 0.12 percentage point. The major sources of the decrease were: processed food (0.37 percentage point), Education (0.18 percentage point), clothing & foot wear (0.06 percentage point), and Alcoholic Beverages, Tobacco & Kola (0.01 percentage point). All other components of core inflation increased in the reviewed period (Table 3.6 and Figure 3.8). The substantial drop in the prices of processed food and Education which drove the decline in core inflation was traceable to the pass-through effect of the stability in the exchange rate to lower domestic prices on account of the Bank's recent foreign exchange management measures, particularly, the establishment of the I&E window and improved funding of BDCs.

Table 3.6
Major Components of Core Inflation
(Y-on-Y) July – Dec. 2017

CORE INFLATION	July	August	September	October	November	December	Change btw July and December
Core Inflation	12.21	12.30	12.12	12.14	12.21	12.09	-0.12
Processed Food	6.02	6	5.9	5.85	5.81	5.65	-0.37
Milk, cheese and egg	0.38	0.38	0.38	0.39	0.39	0.25	-0.13
Sugar, Jam, Honey, etc	0.19	0.2	0.2	0.2	0.21	0.1	-0.09
Non-Alcoholic Bev	0.19	0.20	0.2	0.21	0.21	0.21	0.02
Alcoholic Bev.,Tobacco & kola	0.12	0.12	0.12	0.11	0.11	0.11	-0.01
Clothing and footware	1.7	1.72	1.7	1.69	1.68	1.64	-0.06
Housing, Water, Elect. Gas &other Fuels	0.36	0.44	0.47	0.51	0.58	0.62	0.26
Furnishings, HH Equipments & M	0.85	0.89	0.9	0.92	0.93	0.94	0.09
Health	0.45	0.47	0.46	0.47	0.48	0.49	0.04
Transport	1.11	1.12	1.11	1.14	1.15	1.17	0.06
Communication	0.02	0.02	0.02	0.02	0.02	0.02	0
Recreation and Culture	0.08	0.08	0.08	0.08	0.07	0.07	-0.01
Education	0.81	0.76	0.69	0.65	0.64	0.63	-0.18
Restaurant & Hotel	0.2	0.20	0.19	0.2	0.21	0.22	0.02
Misc Goods and Services	0.29	0.30	0.29	0.3	0.31	0.32	0.03

Figure 3.6
Major Components of Core Inflation
(Y-on-Y) July – Dec. 2017

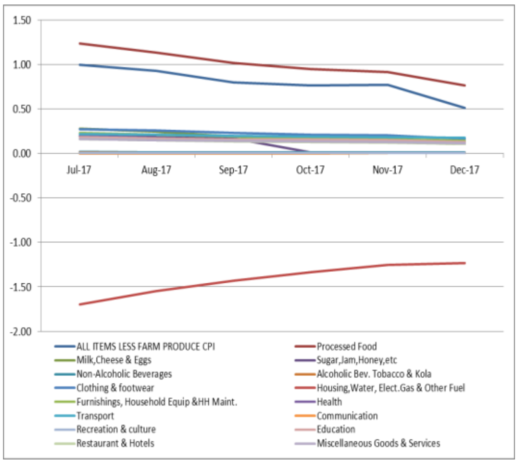


On a month-on-month basis, core inflation decreased by 0.49 percentage point from 1.00 per cent in July to 0.51 per cent in December 2017. Processed food remained the major driver of the decline in core inflation, decreasing from 1.24 per cent in July to 0.77 per cent in December 2017. This was followed by clothing and foot wear (-0.12 percentage point), Furnishing and Household Equipment & maintenance (-0.09 percentage point), Health (-0.08 percentage point), Education (-0.05 percentage point) and Restaurant and Hotels (-0.05 percentage point) (Table 3.7 and Figure 3.9).

Table 3.7
Major Components of Core Inflation (M-on-M) July – Dec. 2017

	July	August	September	October	November	December	Change btw July and December
Core Inflation	1.00	1.00	0.80	0.76	0.77	0.51	-0.49
Processed Food	**1.24**	**1.24**	**1.02**	**0.95**	**0.91**	**0.77**	-0.47
Milk, cheese and egg	0.17	0.17	0.14	0.13	0.13	0.00	
Sugar, Jam, Honey, etc	0.02	0.02	0.01	0.01	0.01	0.00	
Non-Alcoholic Bev	0.02	0.02	0.01	0.01	0.01	0.01	-0.01
Alcoholic Bev.,Tobacco & kola	0.01	0.01	0.01	0.01	0.01	0.01	0.00
Clothing and footware	0.28	0.28	0.23	0.21	0.20	0.16	-0.12
Housing, Water, Elect. Gas &other Fuels	-1.70	-1.70	-1.43	-1.34	-1.25	-1.23	0.47
Furnishings, HH Equipments & M	0.23	0.23	0.19	0.17	0.16	0.14	-0.09
Health	0.20	0.20	0.15	0.14	0.14	0.12	-0.08
Transport	0.22	0.22	0.19	0.19	0.18	0.18	-0.04
Communication	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Recreation and Culture	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Education	0.18	0.18	0.16	0.16	0.15	0.13	-0.05
Restaurant & Hotel	0.16	0.16	0.13	0.13	0.12	0.11	-0.05
Misc Goods and Services	0.16	0.16	0.14	0.13	0.13	0.11	-0.05

Figure 3.7
Major Components of Core Inflation (M-on-M) July – Dec. 2017



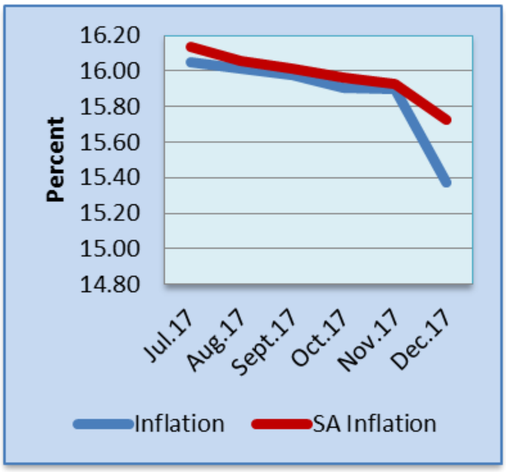
3.1.4 Seasonally-Adjusted Inflation

The actual and seasonally-adjusted measures of headline inflation trended downwards in the review period, continuing the trend of decline witnessed towards the end of first half of 2017 (Table 3.8 and Figure 3.10). Actual headline inflation continued to reflect the general price level in the economy, trending below the seasonally-adjusted headline inflation throughout the second half of 2017. The overall downward trend in both actual and seasonally-adjusted measures of inflation were attributed to the stability in the foreign exchange market, improved accretion to external reserves and increased food production partly arising from the Anchor Borrowers' Programme.

Table 3.8
Actual and Seasonally Adjusted Headline Inflation July -December 2017

Date	Inflation	SA Inflation
Jul.17	16.05	16.13
Aug.17	16.01	16.05
Sept.17	15.98	16.01
Oct.17	15.91	15.97
Nov.17	15.9	15.93
Dec.17	15.37	15.73

Figure 3.8
Actual and Seasonally Adjusted Headline Inflation July - December 2017



3.2 Key Factors that Influenced Domestic Prices

The behaviour of inflation during the review period was driven by cost-push, demand-pull and moderating factors. The net effect of these forces gave rise to the moderation in inflation experienced in the period. A highlight of these factors are: the stability in the exchange rate, sustained tight monetary policy stance, improved agricultural harvests, sustained interventions by the Bank to support the real sector, weak aggregate demand resulting from unpaid workers salaries and contractor debts, and relative stability in energy prices which, however, gave way to some fuel shortages towards the end of the period. Others included: the liquidity effects of the bailout of state governments; increased government spending to support the expansionary 2017 Federal Government budget; the impact of festive and other seasonal activities; worsening conflicts between herdsmen and farmers in many parts of the country as well as disruption to production and distribution activities due to insurgency in the North East.

3.2.1 Demand-side Factors

The moderation in headline inflation was largely attributed to the continued tight monetary policy stance of the Bank, which helped to rein-in inflationary pressures. Also, the Bank's foreign exchange demand management measures substantially moderated exchange rate depreciation, leading to stability in the exchange rate with pass-through to lower domestic prices. In addition, weak aggregate demand arising from unpaid workers salaries and outstanding contractors debt as well as relative stability in energy prices, further helped in moderating the pressure on the domestic price level.

3.2.2. Supply-Side Factors

Some supply side factors moderated inflation in the review period, while others dampened the moderation. The year 2017 enjoyed relatively clement weather conditions resulting in improved agricultural harvests, thereby dampening the pressure on food prices. This was supported by the Bank's sustained interventions in the real sector. Also, the increase in electricity generation by 5.60 per cent to 3,875.3MW in the fourth quarter of 2017 helped to moderate the domestic price level. On the other hand, the continued conflicts between herdsmen and farmers which affected farming activities and reduced productivity, continuing insurgency in the North East region as well as perennial challenges of poor infrastructure, mitigated the moderation in inflation rates.

3.2.3 Moderating Factors

In the second half of 2017, the factors that moderated domestic prices included stable supply of foreign exchange in the market and moderated energy prices. Other factors were the modest resumption in farming activities and the rebuilding of damaged distribution chains in the North-East following the success recorded in the campaign against insurgency. In addition, the introduction of the Economic Recovery and Growth Plan provided a strategic roadmap for the economy and helped restore investor confidence.

CHAPTER FOUR

4.0 MONETARY POLICY AND LIQUIDITY MANAGEMENT

Developments in the global and domestic economic and financial environments continued to pose challenges to monetary policy in the second half of 2017. On the global front, the continued slow pace of recovery in global oil and other commodity prices, the damage to infrastructure caused by hurricanes - Harvey, Irma and Maria, the reduction in China's uptake of global commodities, and financial market uncertainties due to monetary policy normalization in the US were the key challenges to output recovery. These were compounded by trade protectionism and immigration challenges, complexities arising from the BREXIT negotiations, continued tensions on the Korean Peninsula as well as geo-political risks associated with the growing right-wing political movements in Europe. Emerging market and developing economies continued to witness strong economic headwinds, although Brazil, South Africa and Nigeria exited recession.

On the domestic front, the key challenges that confronted monetary policy were: the high but moderating inflationary pressure with strong base effect; fragile growth recovery; threats to financial system stability from banking system liquidity surfeit, and weakening macro-prudential indicators. Others included: sustaining the fragile stability in the foreign exchange market; contraction in private sector credit; high unemployment rate; rising costs and shortages of energy; rising debt profile of the Federal and sub-national governments and the uncertainty surrounding the late passage and implementation of the 2017 Federal Government budget. Against this background, the Bank's desire to support the fragile recovery from recession, without compromising the achievement of price and exchange rate stability, shaped monetary policy decisions during the review period.

4.1 DECISIONS OF THE MONETARY POLICY COMMITTEE (MPC)

The decisions of the Monetary Policy Committee (MPC) in the review period were influenced by key global and domestic economic and financial developments. The key global developments were: the continuing wave of protectionist sentiments, heightened geo-political tensions, continued fragilities in financial markets and slow pace of recovery in oil and other commodity prices.

On the domestic front, the key concerns were: fragile economic recovery, the high but moderating inflationary pressure with strong base effect, weak aggregate demand, low fiscal buffers, threats to financial system stability from banking system liquidity surfeit and weakening macro-prudential indicators. These challenges and the need to achieve the Bank's mandate provided the context for monetary policy decisions.

4.1.1 July 2017 MPC Meeting

The 24th and 25th July, 2017 Monetary Policy Committee (MPC) meeting reviewed key developments in the global and domestic economic and financial environments in the first half of 2017 and the outlook for the rest of the year.
At the global stage, the key developments were: relatively improving global economic outlook, strengthening commodity prices and positive macroeconomic outcomes in the advanced economies with spillovers to the emerging markets and developing economies. Trade protectionism and immigration challenges, fragilities in the financial markets, receding market expectations of expansionary U.S. fiscal policy as well as weaker-than-expected growth in the U.K due to difficult BREXIT negotiations, however, remained key risks to global economic stability.

On the domestic front, the Committee noted that the contraction in the economy moderated to 0.52 per cent in Q1 2017 from 1.30 per cent in Q4 2016, with fifteen economic activities recording positive growth. The economy showed strong signs of recovery, as non-oil real GDP grew by 0.72 per cent in Q1 2017, reflecting growth in the agricultural sector of 0.77 per cent in the same period. The Committee also noted the continued positive effects of improved foreign exchange management on the performance of manufacturing and other economic activities.

In terms of price developments, headline inflation (year-on-year) declined for the fifth consecutive month in June 2017, to 16.10 per cent from 16.25 per cent in May and 18.72 per cent in January 2017. The Committee partly attributed the moderation in inflation to the effects of the relative stability in the foreign exchange market, arising from improved management, which encouraged foreign inflows. The Committee observed that while the moderation in inflation was broadly in response to the prevailing tight monetary policy stance, the base effect was still strong but could wane by August 2017. The MPC also welcomed improvements in the equities segment of the capital market as the All-Share Index (ASI) and stock Market Capitalization (MC) rose by 33.33 and 32.84 per cent, respectively, between March 31 and July 21, 2017, reflecting growing investor confidence.

The Committee also reviewed available forecasts of key macroeconomic indicators which largely pointed to fragile economic recovery in the second quarter of the year. Accordingly, the MPC cautioned that this delicate recovery could relapse into a protracted recession if strong and bold monetary and fiscal policies were not immediately activated. In this regard, the MPC urged the fiscal authorities for a timely implementation of the 2017 budget and the Economic Recovery and Growth Plan (ERGP) in order to sustain the recovery, stimulate employment, further strengthen growth, and restore confidence in the economy. Consequently, the Committee identified the downside risks to the outlook to include: weak financial intermediation, poorly targeted fiscal stimulus and the absence of structured programme implementation.

At that meeting therefore, the broad policy consideration of the Committee was either to hold or ease position. The argument for holding was largely premised on the need to safeguard the stability so far achieved in the foreign exchange market and allow time for previous policy measures to work through the economy. Specifically, the MPC considered the high level of banking system liquidity; the need to continue to attract foreign inflows to support the foreign exchange market and economic activity; the expansive outlook for fiscal policy in the rest of the year; and the prospective election-related spending which could increase system liquidity.

In contrast, the argument for easing was the need for the Committee to signal its sensitivity to growth and employment concerns by encouraging the flow of credit to the real economy. Also, easing at this time would reduce the cost of debt service, which is actually crowding out government expenditure. The risks to easing, however, would show up in terms of upstaging the modest stability achieved in the foreign exchange market, through the likely exit of foreign portfolio investors as well as a resurgence of inflation following the intensified implementation of the 2017 budget in the course of the year. The Committee also reasoned that easing would pull the real interest rate further into the negative territory.

On balance and in consideration of the challenges confronting the domestic economy as well as uncertainties in the global environment, the Committee decided by a vote of 6 to 2 members to retain the Monetary Policy Rate (MPR) at 14.0 per cent alongside all other policy parameters. In summary, the MPC voted to: Retain the MPR at 14 per cent; Retain the CRR at 22.5 per cent; Retain the Liquidity Ratio at 30.00 per cent; and Retain the Asymmetric corridor of +200 and -500 basis points around the MPR.

4.1.2 September 2017 MPC Meeting

At the 25th and 26th September, 2017 MPC meeting, the Committee observed that global output growth was projected to improve to 3.5 per cent in 2017 from 3.2 per cent in 2016, with major emerging market and developing economies including Nigeria, Brazil and South Africa exiting recession. The key challenges to global recovery prospect were identified to include: recent developments on the Korean peninsula; the damage to infrastructure caused by hurricanes - Harvey, Irma and Maria; the lull in BREXIT negotiations and the normalization of monetary policy by the US Fed, expected to instigate global capital flow reversal as well as the slow pace of recovery in oil and other commodity prices, and China's reduction in uptake of global commodities.

On the domestic scene, data from the National Bureau of Statistics (NBS) showed that real Gross Domestic Product (GDP) grew by 0.55 per cent in the second quarter of 2017, reversing the contractions of 0.91 and 1.49 per cent in the previous quarter, and the corresponding period of 2016, respectively. The Committee welcomed this development which effectively marked the country's technical exit from recession. It further noted that, although the recovery was weak, the active implementation of the 2017 budget could hopefully boost aggregate demand and employment to strengthen growth.

In terms of price developments, the Committee observed that the economy continued on the path of disinflation with headline inflation (year-on-year) moderating for the seventh consecutive month to 16.01 per cent in August 2017, from 16.05 per cent in July 2017. The outcome was attributed to the contraction in money supply, decline in imported food and non-food prices, favourable base effects, and the moderating effects of stable exchange rates.

The financial market also remained relatively stable, buoyed by the continuing improvement in the external reserves position and developments in the equities segment of the capital market. External reserves position grew to US$32.9 billion on 25th September, 2017 while the All-Share Index (ASI) and stock Market Capitalization (MC) rose by 7.20 and 6.90 per cent, respectively, between June 30 and August 31, 2017, reflecting continuing investor confidence, following improvements in foreign exchange management.

The Committee's considerations at this meeting centered on output and price developments. In terms of output, the MPC noted the economy's exit from recession, although the growth remained fragile. It hoped that complementary fiscal and monetary policy measures would be required to support the growth momentum. The Committee further expressed satisfaction with the gradual, but consistent decline in inflation, noting, however, the underlying base effect in addition to the continued improvement in the naira exchange rate across all segments of the foreign exchange market.

In arriving at a decision, the Committee took note of the gains so far achieved from its earlier decisions; including the stability in the foreign exchange market and the moderate reduction in inflation. Accordingly, the broad policy options facing the Committee were either to tighten, ease or hold. Although tightening would help rein-in inflation expectations and strengthen the stability in the foreign exchange market, the Committee felt that this option would further widen the income gap, depress aggregate demand and adversely affect credit delivery to the private sector. The Committee also noted that tightening may result in the deposit money banks re-pricing their assets, thus raising the cost of borrowing and worsening the already weak investment climate and non-performing loans.

The argument for easing was that this option would make it more attractive for Nigerians to acquire assets at cheaper prices, thus increasing their net wealth, and, therefore, stimulate spending as confidence rises. Nevertheless, the Committee felt concerned that loosening at this time would exacerbate the inflationary pressures and worsen exchange rate depreciation. The Committee also felt that loosening will pull the real interest rate deeper into negative territory as the gap between the nominal interest rate and inflation widens.

The argument for holding was premised on maintaining stability to allow the effect of recent policy measures to take root. In particular, the Committee felt that the effects of fiscal policy actions towards stimulating the economy have begun to manifest as evident in the exit of the economy from the fifteen-month recession. Also, the fragility of the growth recorded makes it imperative to allow more time to take appropriate complementary policy decisions to strengthen the recovery. Overall, the most compelling argument for a hold was to achieve greater clarity in the evolution of key macroeconomic indicators including budget implementation, economic growth, exchange rate, inflation and employment generation.

In consideration of the headwinds confronting the domestic economy and the uncertainties in the global environment, the Committee voted to: Retain the MPR at 14.0 per cent; Retain the CRR at 22.5 per cent; Retain the Liquidity Ratio at 30.0 per cent; and Retain the Asymmetric corridor of +200 and -500 basis points around the MPR.

4.1.3 November 2017 MPC Meeting

The 20th and 21st November, 2017 MPC meeting noted the improving global growth prospects as reflected in the revision of global output growth for 2017 to 3.6 from 3.5 per cent up from 3.2 per cent in 2016. The revision of global growth was premised on the uptick in global economic activity, strengthened by the recovery in oil and other commodity prices, and improved aggregate demand. The MPC, however, identified the risks to the revised outlook for global growth to include: continued tension on the Korean Peninsula, complexities arising from the BREXIT negotiations and financial market uncertainties due to monetary policy normalization in the US. The Committee also noted a slow pace of inflation trajectory in most advanced economies and the abatement of inflationary pressures in some key emerging market economies, as they exit recession and their currencies stabilize. Accordingly, the outlook for global monetary policy remained largely accommodative, in support of economic recovery and growth.

At the domestic front, data showed that real Gross Domestic Product (GDP) grew by 1.40 per cent in the third quarter of 2017, up from 0.72 per cent, and contraction of 0.91 per cent in the second and first quarter of 2017, respectively. The Committee noted with satisfaction the second consecutive quarterly growth in real GDP following five quarters of contraction. The Committee also noted that the growth was largely driven by the oil sector as non-oil real GDP contracted by 0.76 per cent in Q3 2017, giving credence to the need to put in place policies to boost non-oil growth and consolidate the recovery. Overall, the Committee noted that the economy has begun to show strong signs of recovery as public investment had picked up with increased housing construction at the Federal and state levels, as well as shipping activities at the ports.

On price development, the Committee noted the continued moderation in headline inflation (year-on-year) for the ninth consecutive month to 15.91 per cent in October 2017 from 15.98 per cent in September 2017. The Committee attributed the development to contraction in money supply, favourable but dwindling base effect, and the relatively stable naira exchange rate. In spite of the marginal decline in food inflation in October, the Committee noted that the rate remained high, traceable to supply shortages exacerbated by cross-border sales and distribution bottlenecks as well as high prices of farm inputs.

The Committee was satisfied with the sustained stability in the financial markets as reflected in relative stability in the exchange rate, continuing improvement in the level of external reserves and the equities segment of the capital market. The Committee noted the gradual convergence between the rates in the Bureau de change (BDC) and the Nigerian Autonomous Foreign Exchange Market (NAFEX) segments as well as stability in the interbank segment of the market. The MPC equally welcomed the growing patronage at the Investors' and Exporters' window of the foreign exchange market, reflecting the growing confidence of foreign and local investors. The All-Share Index (ASI) and stock Market Capitalization (MC) rose by 3.38 and 4.35 per cent, respectively, between August 31 and November 17, 2017, indicating sustained investor confidence, due to improvements in foreign exchange supply.

On financial stability, the Committee observed that the overall condition and outlook for the banking system was stable as deposit money banks' balance sheets remained strong, although it noted the concentration of non-performing loans in a few sectors. Nonetheless, the Committee urged further strengthening of supervisory oversight and deployment of early warning systems in order to promptly identify vulnerabilities and proactively manage emerging risks to banking system stability.

In arriving at its decision, the Committee appraised potential policy options in terms of their balance of risks, against the backdrop of the gains so far made from earlier policy decisions. These included: the stability in the foreign exchange market and the moderate reduction in inflation. Thus, the policy options at this meeting were either to hold, tighten or ease policy stance.

While tightening would strengthen the impact of monetary policy on inflation with complementary effects on capital inflows and exchange rate stability, it nevertheless could also potentially dampen the positive outlook for growth and financial system stability. On the other hand, loosening would support the outlook for growth by stimulating domestic aggregate demand through reduced cost of borrowing; it could, however, aggravate upward trend in consumer prices and generate exchange rate pressures. The Committee also felt that loosening would worsen the current account balance through increased importation. The argument to hold was predicated on allowing key variables to continue to evolve in line with the subsisting stance of macroeconomic policy. Members noted that the developments in output and inflation, in particular, required close monitoring in order to gain more clarity on the medium term path of monetary policy.
In consideration of the foregoing, the Committee voted to retain the MPR at 14.0 per cent; retain the CRR at 22.5 per cent; retain the Liquidity Ratio at 30.0 per cent; and Retain the Asymmetric corridor of +200 and -500 basis points around the MPR.

4.2 Instruments of Liquidity Management

In order to achieve its objectives of price and monetary stability, the Bank continued to employ various policy instruments in its tool kit in the review period. The instruments deployed were: the Monetary Policy Rate (MPR), Cash Reserve Ratio (CRR), Liquidity Ratio (LR), Open Market Operations (OMO), and Discount Window Operations complemented by interventions in the foreign exchange market.

4.2.1 Monetary Policy Rate (MPR)

The MPR remained the key instrument of monetary policy in the review period. The MPR was maintained at 14.0 per cent throughout the period along with the asymmetric corridor of +200 and -500 basis points around the MPR. The retention of the MPR and its asymmetric corridor signaled the Bank's commitment to sustain the macroeconomic stability so far achieved.

4.2.2 Open Market Operations (OMO)

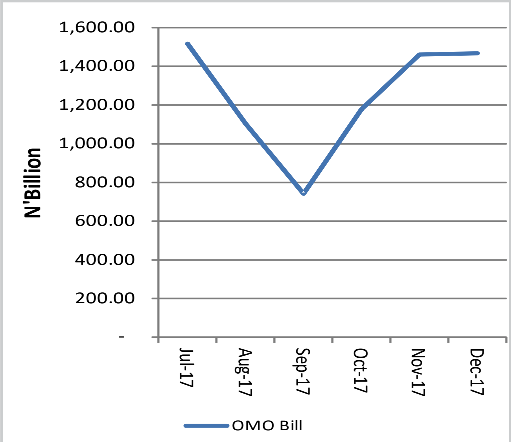
The Bank increased its reliance on Open Market Operations (OMO) as the main avenue for managing banking system liquidity in the second half of 2017. As a result, total OMO sales rose significantly by 92.87 per cent to ₦7,472.21 billion in the second half from ₦3,874.27 billion in the first half of 2017. The increase in OMO sales in the second half of 2017 was to reduce the level of liquidity in the banking system in order to moderate inflationary pressures, in line with the prevailing tight monetary policy stance of the Bank. On a year-on-year basis, OMO sales increased by 35.12 per cent above the level in the second half of 2016 (Table 4.1).

Table 4.1
OMO Bills Auction (January 2016 – December 2017) (₦'million)

Date	2016	2017	% Change
Jan	698.42	700.52	
Feb	509.23	619.14	
Mar	394.63	391.16	
Apr	363.72	316.09	
May	64.63	580.08	
Jun	299.12	1,267.28	
1st Half	**2,329.75**	**3,874.27**	**66.30**
Jul	695.21	1,517.53	
Aug	1,728.15	1,104.57	
Sep	1,057.95	741.85	
Oct	807.02	1,179.20	
Nov	665.57	1,461.13	
Dec	575.97	1,467.93	
2nd Half	**5,529.87**	**7,472.21**	**35.12**
Cumulative Figure	**7,859.62**	**11,346.48**	**44.36**

Source: Financial Market Department, CBN

Figure 4.1
OMO Bills Auction (July – December 2017)



4.2.3 Reserve Requirements

To complement MPR and OMO as instruments of liquidity management, the Bank also used macro-prudential requirements namely: the cash reserve ratio (CRR) and liquidity ratio (LR) in the second half of 2017. During the period, the CRR was retained at 22.5 per cent to address the excess liquidity condition in the banking system. Also, the liquidity ratio was unchanged at 30.0 per cent in the second half of 2017.

4.2.4 Standing Facilities

In the second half of 2017, the Bank continued to deploy the standing facilities (lending/deposit) window to meet daily liquidity requirements of Deposit Money Banks (DMBs) and the

Discount House (DH). The asymmetric corridor of +200/-500 basis points around the MPR, which defined the standing facilities, was maintained throughout the review period.

At the Standing Lending Facility (SLF) window, the requests decreased by 6.56 per cent to ₦25,664.35 billion in the second half of 2017 from ₦27,466.58 billion in the first half. This, however, represented a 621.80 per cent increase compared with N3,555.62 billion in the corresponding period of 2016 (Table 4.2).

The volume of deposits at the Standing Deposit Facility window also decreased by 22.42 per cent to ₦4,274.99 billion in the second half from ₦5,510.75 billion in the first half of 2017. This represented a 28.33 per cent decrease relative to the corresponding period of 2016 (Table 4.3). The transactions at the two windows resulted in a net lending of N21,389.36 billion in the second half of 2017, slightly down from N21,955.83 billion in the first half. The development could partly be attributed to DMBs perverse incentives whereby funds sourced at the CBN window find their way into the foreign exchange market, although the Bank has a subsisting regulation on this unhealthy practice.

Table 4.2
CBN Standing Lending Facility (January 2016 – December 2017) (₦'billion)

Date	2016	2017	% Change
Jan	84.26	3,380.57	
Feb	4.11	4,478.50	
Mar	474.75	5,052.56	
Apr	942.66	5,746.68	
May	869.52	4,596.99	
Jun	2,762.36	4,211.28	
1st Half	**5,137.66**	**27,466.58**	**434.61**
Jul	2,727.21	3,855.13	
Aug	4,255.97	5,585.51	
Sep	3,482.35	4,377.89	
Oct	4,132.39	5,605.30	
Nov	5,041.36	3,909.09	
Dec	3,820.61	2,331.43	
2nd Half	**3,555.62**	**25,6[illegible]**	**621.80**
Total	**8,693.28**	**53,130.92**	**511.17**

Source: Financial Market Department

Figure 4.2
CBN Standing Lending Facility (July – December 2017)

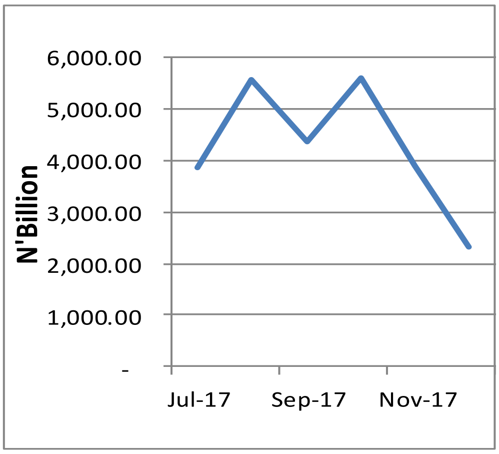


Figure 4.3
CBN Standing Facility (July – December 2017)

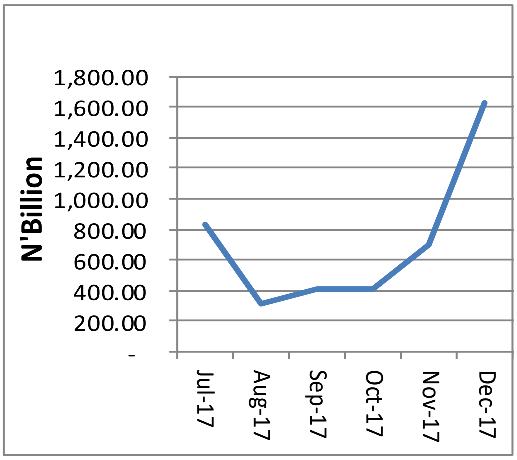


Table 4.3
CBN Standing Deposit Facility (January 2016 – December 2017) (N'billion)

Date	2016	2017	% Change
Jan	2,369.31	1,855.98	
Feb	2,553.89	804.07	
Mar	1,635.43	889.35	
Apr	2,971.33	593.79	
May	1,760.02	665.28	
Jun	1,822.25	702.28	
1st Half	**13,112.23**	**5,510.75**	**57.97**
Jul	934.29	825.10	
Aug	1,050.27	315.24	
Sep	826.94	411.43	
Oct	949.32	405.21	
Nov	744.30	691.97	
Dec	1,459.81	1,626.05	
2nd Half	**5,964.93**	**4,274.99**	**28.33**
Total	**19,077.16**	**9,785.74**	**48.70**

Source: Financial Market Department

4.2.5 Foreign Exchange Intervention

During the review period, the Bank continued to intervene in the foreign exchange market in order to sustain the stability so far achieved and strengthen the gains recorded in the investors' and exporters' foreign exchange window. Additional reforms and interventions during the period were aimed at encouraging capital inflows to improve liquidity in the market. These measures were the intensification of the policy on repatriation of export proceeds as well as return of unutilized foreign exchange sourced from CBN auctions. The Bank also sustained the implementation of existing measures including: the restriction of access to foreign exchange for 41 items, the use of Bank

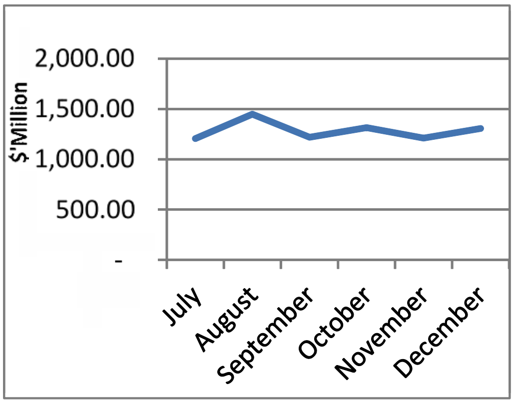
Verification Number (BVN) in BDC transactions, resumption of sale of foreign exchange by the Bank and International Money Transfer Operators (IMTOs) to BDCs, as well as special foreign exchange auction to targeted sectors and foreign exchange sales for small scale importation. As a consequence, the rates at the bureau-de-change (BDC) and Nigeria Autonomous Foreign Exchange (NAFEX) segments moved towards convergence as demand pressure in the market moderated. In addition, the average naira exchange rate at the inter-bank segment of the foreign exchange market remained stable in the second half of 2017.

Consequently, total supply of foreign exchange declined by 5.11 per cent to US$7,710.49 million in the second half of 2017 from US$8,125.95 million in the first half. This, however, represented an increase of 162.26 per cent compared with US$2,940.05 million in the corresponding period of 2016 (Table 4.4). The year-on-year increase in the supply of foreign exchange largely reflected improved autonomous inflows and accretion to external reserves. These helped to stabilize the exchange rate and restore investor confidence in the Nigerian economy.

Table 4.4
Foreign Exchange Supply by the CBN (US$ Million)

	2016	2017
	Total FX Supply (Including Forward Sales ($'Million))	Total FX Supply (Including NAFEX and Forward Sales ($'Million))
January	973.57	789.76
February	895.77	876.48
March	1,093.05	1,309.44
April	727.69	1,919.30
May	617.50	2,109.93
June	1,423.81	1,121.04
1st Half	**5,731.40**	**8,125.95**
July	470.00	1,207.00
August	576.15	1,449.49
September	105.00	1,220.33
October	343.92	1,315.99
November	363.11	1,210.99
December	1,081.87	1,306.69
2nd Half	**2,940.05**	**7,710.49**
Total	**8,671.45**	**15,836.44**

Figure 4.4
Total FX Supply (Including NAFEX and Forward Sales ($'Million)



4.3. Developments in the Monetary Aggregates

In the second half of 2017, monetary aggregates performed better than in the first half, even though most of the aggregates did not meet their targets at end-December 2017. The development was due to the decline in net domestic assets (NDA), following the contraction in credit to government which was, however, moderated by increase in net foreign assets (NFA) during the review period.

4.3.1 Broad Money (M2)

Broad Money (M2) grew by 9.19 per cent to ₦24,001.41 billion at end-December 2017 from ₦21,980.58 billion at end-June 2017. Compared with the end-December, 2016 level of ₦23,591.73 billion, M2 increased by 1.74 per cent. The year-on-year growth of 1.74 per cent in M2 was significantly below the 2017 indicative growth target of 10.29 per cent.

Figure 4.5
Money Supply (M1) and (M2) (July – December, 2017)

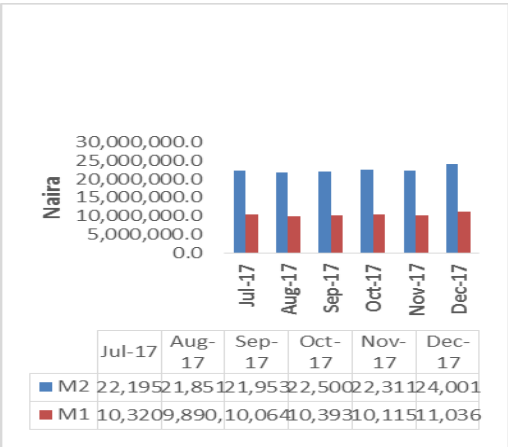
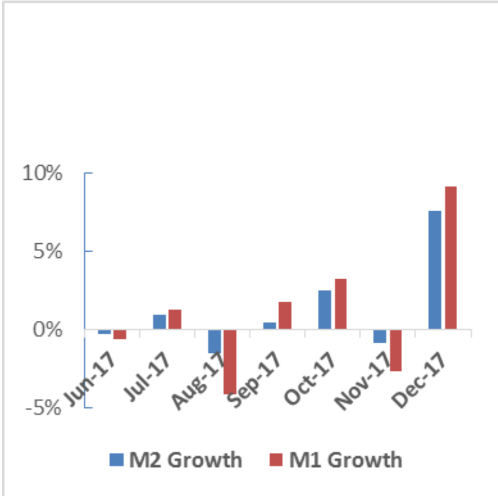


Figure 4.6
Growth in Money Supply (M1) and (M2) (June - December, 2017)



4.3.2 Narrow Money (M1)

Narrow Money (M_1), grew by 8.30 per cent to ₦11,036.35 billion at end-December 2017, from ₦10,190.19 billion at end-June 2017. When compared with the end-December 2016 figure of ₦11,271.50 billion, M1 contracted by 2.09 per cent. The year-on-year contraction in M1 of 2.09 per cent was below the indicative growth target of 11.07 per cent (Figures 4.4 and 4.5), indicating that M1 under-performed during the review period. The year-on-year contraction in M1 is traceable to the contractions of 2.07 and 2.09 per cent in both currency outside bank and demand deposit from ₦1,820.42 billion and ₦9,451.09 to ₦1,782.66 billion and ₦9,253.69 billion, respectively, over the same period.

4.3.3 Net Foreign Assets (NFA)

Net Foreign Assets (NFA) increased by 74.93 per cent to ₦ 14,813.28 billion at end-December 2017 from ₦8,468.08 billion at end-June 2017. Compared with the end-December 2016 figure of ₦ 9,149.66 billion, NFA grew by 61.90 per cent. This year-on-year increase in NFA of 61.90 per cent was above the indicative growth target of -29.31 per cent, attributed to recovery in crude oil prices and sustained capital inflows as economic fundamentals improved.

4.3.2 Net Domestic Assets (NDA)

Net Domestic Credit (NDC) contracted by 5.04 per cent to ₦25,863.28 billion at end-December 2017 from ₦27,236.43 billion at end-June 2017. Compared with the end-December 2016 level of ₦26,857.72 billion, NDC contracted by 3.07 per cent, as against the indicative growth target of 17.93 per cent, largely on account of huge contraction in credit to government.

Figure 4.7
Net Domestic Asset (NDA) (July - December 2017)

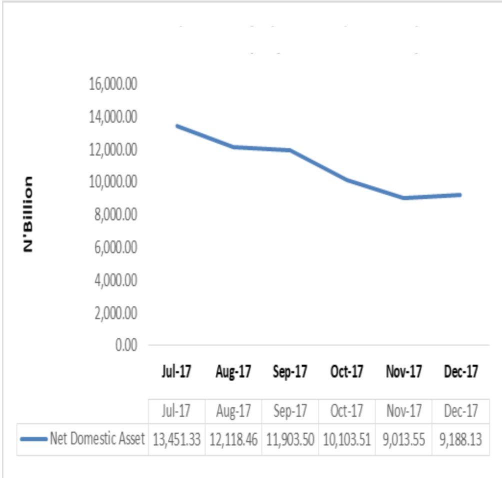
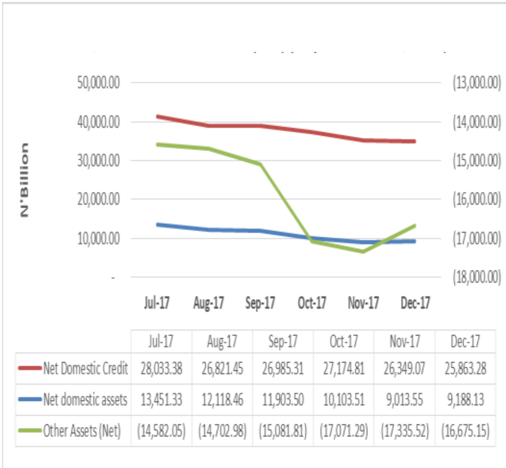


Figure 4.8
NDA, NDC and Other Assets (Net) (July – December, 2017)



4.4.3 Credit to the Government (C_g)

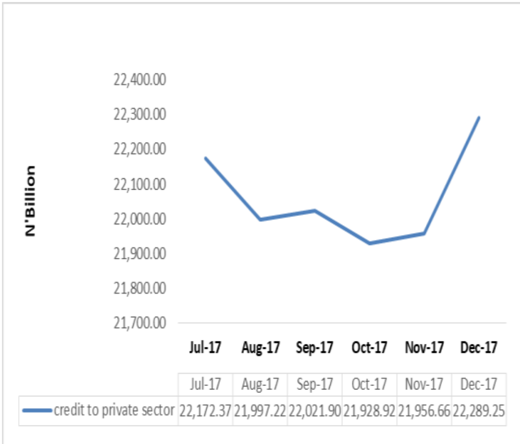
Credit to government (Cg) in the second half of 2017 contracted by

31.93 per cent to ₦3,574.03 billion at end-December 2017 from ₦5,250.49 billion at end-June 2017. Credit to government also contracted year-on-year by 26.70 per cent when compared with the end-December 2016 figure of ₦4,875.57 billion. This was in contrast to the indicative growth benchmark of 32.99 per cent. The development was attributed to improved oil receipts occasioned by higher oil prices and government's recent policy of increased reliance on foreign borrowings.

4.4.4 Credit to the Private Sector (C_p)

Credit to the private sector (C_p) increased by 1.38 per cent to ₦22,289.25 billion at end-December 2017 from ₦21,985.95 billion at end-June 2017. Compared with the end-December 2016 figure of ₦21,982.15 billion, C_p rose marginally by 1.40 per cent, which was, significantly below the indicative growth target of 14.89 per cent for 2017. The slow performance of credit to the private sector in the review period was attributed to the reluctance of DMBs to create credit due to weak macroeconomic conditions as reflected in the fragile growth rate of the economy. The CBN and Commercial banks' components of credit to the private sector rose by 3.11 and 0.63 per cent to ₦5,869.29 billion and ₦16,193.86 billion at end-December 2017 from ₦5,692.29 billion and ₦16,092.23 billion, respectively, at end-June 2017. On a year-on-year basis, the monetary authority's component grew by 155.40 per cent from ₦2,298.26 billion in the corresponding period of 2016, while commercial bank's component declined by 1.86 per cent from ₦16,500.15 billion at end-December 2016.

Figure 4.9
Domestic Credit to Private Sector (July – December, 2017)



4.4.5 Reserve Money (RM)

Reserve Money (RM) increased by 18.20 per cent to ₦6,477.60 billion at end-December 2017, from ₦5,480.21 billion at end-June 2017. Compared with its end-December 2016 level of ₦ 5,847.92 billion, RM increased by 8.53

per cent and was marginally below the indicative benchmark of ₦6,605.50 billion. The year-on-year increase in reserve money is traceable to the growth of 17.76 per cent in bank reserves from ₦3,668.74 billion at end-December 2016 to ₦4,320.37 billion at end-December 2017. Currency in circulation, however, declined by 1.01 per cent from N2,179.17 billion at end-December 2016 to N2,157.23 billion at end-December 2017. The year-on-year growth in RM during the period was attributed to increase in economic activities, following the recovery.

A summary of the major monetary aggregates and the provisional outcomes as at end-December 2017 is presented in Table 4.5.

CHAPTER FIVE

5.0 DEVELOPMENTS IN THE FINANCIAL MARKETS

In the second half of 2017, developments in the Nigerian financial markets were generally influenced by a number of global and domestic economic conditions. On the global scene, although financial markets remained moderately calm, it was under threat from uncertainties around NAFTA renegotiations, BREXIT discussions, and the growing share of companies with low investment grade ratings in the advanced economy bond markets. Other challenges included rising asset valuations and higher leverage arising from continued monetary accommodation, spill-over of financial stability risks to the nonbank and market sectors.

On the domestic front, the market noted the key policy thrust of supporting and sustaining the fragile recovery of the economy into growth. Given the pressure on the exchange rate witnessed in the preceding half year, policy measures were needed to relieve this pressure and encourage foreign inflows to stabilize the market. Accordingly, monetary conditions remained non-accommodative in order to address the perennial liquidity surfeit in the banking system. As a result, money market rates fluctuated upwards in response to the Bank's interventions in the foreign exchange market to stabilize the exchange rate, coupled with increased OMO auctions. Activities at the newly introduced Investors' and Exporters' window helped to support foreign exchange liquidity for willing buyers and sellers, thereby absorbing speculative pressures in the market. Thus, the rates at the Bureau-de-Change (BDC) and the Nigeria Autonomous Foreign Exchange (NAFEX) segments moved towards convergence, indicating the narrowing of arbitrage opportunities in the market. The capital market remained largely bullish, reflecting investors' positive sentiments, attributable to generally improving macroeconomic conditions during the period. Consequently, the all-share index (ASI) increased remarkably by 15.48 per cent over the preceding half year, and 42.30 per cent year-on-year.

5.1 The Money Market

In the review period, liquidity conditions in the banking system continued to mirror activities in the money market. Money market rates fluctuated upwards in response to the Bank's interventions in the foreign exchange market to stabilize the exchange rate, coupled with increased OMO auctions. These were, however, moderated by the liquidity impact of the Federation Account Allocation Committee (FAAC) disbursements, release of balance of Paris Club debt refunds, FGN capital releases, Joint Venture Cash (JVC) call payments and maturing CBN bills and government securities. As a result, the Interbank and OBB rates remained largely above the upper band of the standing facilities corridor. In addition, high transaction levels were recorded at the collateralized segment of the money market with several periods of inactivity at the Interbank segment, reflecting heightened counter-party risks during the period.

5.1.1 Short-term Interest Rate Developments

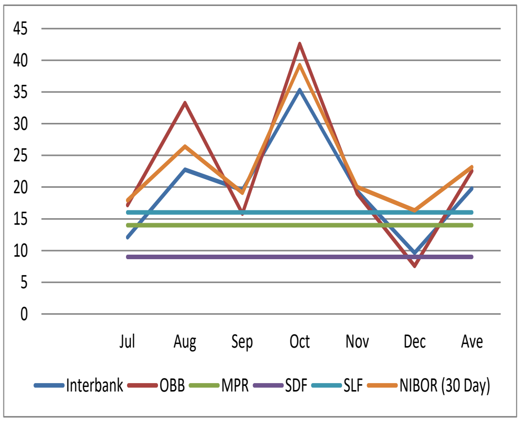
In the second half of 2017, money market rates largely reflected liquidity conditions in the banking system. There was increased transaction in the OBB segment, an indication of the increased risk perception at the Interbank call segment. Accordingly, the average interbank call rate rose from 12.08 per cent in July to 19.55 per cent in September and further to 35.31 per cent in October. It, however, declined to 19.38 per cent in November and 9.64 per cent in December. On the other hand, the average OBB rate fell from 17.18 per cent in July to 15.80 per cent in September. It, however, rose sharply to 42.55 per cent in October, and closed at 7.59 per cent in December 2017. The interbank call rates ranged between 9.64 and 35.31 per cent and averaged 19.78 per cent, while the OBB rate ranged between 7.59 and 42.55 per cent, averaging 22.57 per cent in the period. Thus, the interbank call rate was generally lower than the OBB rate, due to periods of inactivity at the Interbank call segment.

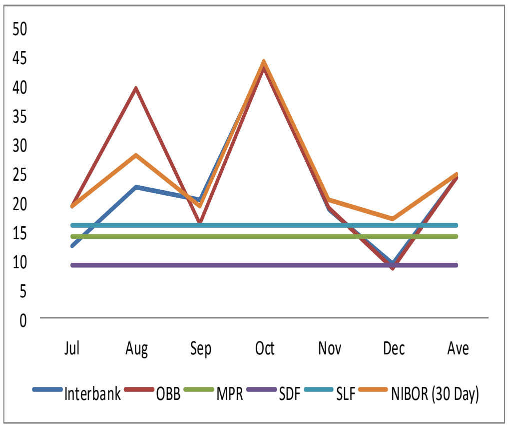
Table 5.1
Weighted Average Monthly Money Market Interest Rates (July –Dec 2017)

Date	Interbank	OBB	MPR	SDF	SLF	NIBOR (30 Day)
Jul	12.08	17.18	14.00	9.00	16.00	17.90
Aug	22.73	33.27	14.00	9.00	16.00	26.38
Sep	19.55	15.80	14.00	9.00	16.00	19.11
Oct	35.31	42.55	14.00	9.00	16.00	39.24
Nov	19.38	19.00	14.00	9.00	16.00	20.02
Dec	9.64	7.59	14.00	9.00	16.00	16.32
Ave	19.78	22.57	14.00	9.00	16.00	23.16

Source: Statistics Dept., (CBN)

Figure 5.1
Weighted Average Monthly Money Market Interest Rates (July –December 2017)

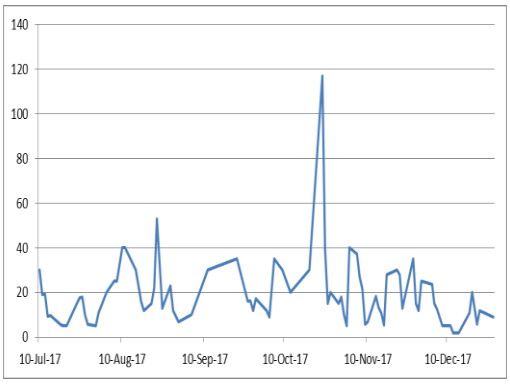




(i) The Interbank Call Rate

During the second half of 2017, the interbank call segment which is the uncollaterized market, recorded several periods of inactivity due to heightened risk aversion amongst DMBs. Theaverage interbank call rate rose from 12.08 per cent in July to 19.55 per cent in September and further to 35.31 per cent in October. It, however, declined to 19.38 per cent in November and 9.64 per cent in December. The interbank call rates ranged between 9.64 and 35.31 per cent and averaged 19.78 per cent, compared with 24.68 per cent in the preceding half year. Analysis of the daily rates showed that the call rate ranged from 2.0 to 116.0 per cent between July and December, 2017. The rate spike of 116.0 per cent recorded in October was due to concerns over liquidity shortages following a court order that DMBs should remit all funds held in accounts without bank verification numbers (BVN) to the Government. The rate, however, declined to 2.0 per cent in December, following improved liquidity conditions and suspension of OMO auctions by the Bank.

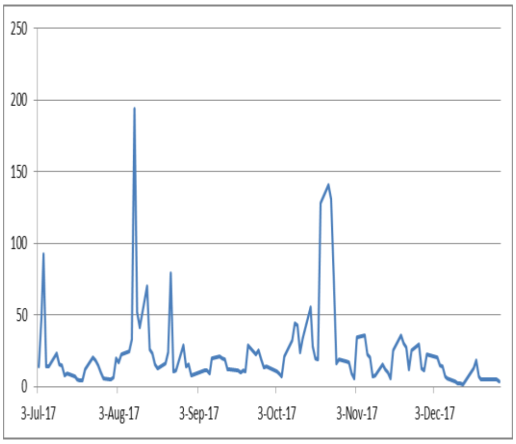
Figure 5.2
Daily Interbank Call Rate (Jul – Dec 2017)



(ii) The Open Buy Back Rate

In the second half of 2017, the OBB segment was more active relative to the interbank call segment. The development largely reflected the increasing risk perception amongst DMBs in view of the impact of the recession on DMBs' assets quality. The average OBB rate fell from 17.18 per cent in July to 15.80 per cent in September. It, however, rose sharply to 42.55 per cent in October, and closed at 7.59 per cent in December 2017. The OBB rate ranged between 7.59 and 42.55 per cent, averaging 22.57 per cent in the period, down from 29.14 in the preceding half year. The daily analysis showed that the OBB rate ranged between 2.00 and 193.95 per cent, with peaks of 92.23, 193.95 and 140.39 per cent in July, August and October, respectively. The peaks reflected liquidity shortages associated with preparation for FAAC meetings and increased OMO auctions. However, it declined significantly in December largely due to liquidity surfeit as CBN suspended the issuance of OMO bills for liquidity management operations.

Figure 5.3
Daily Open Buy Back Rate (July-December 2017)



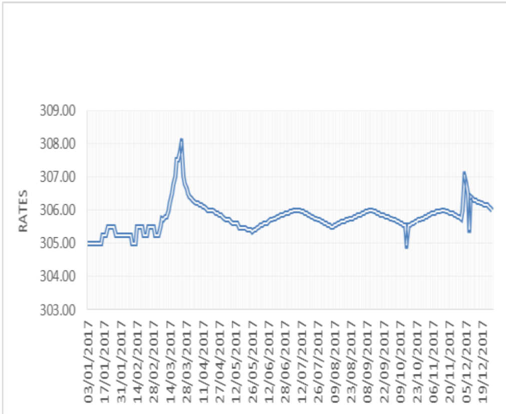
(iii) The Nigeria Interbank Offered Rate (NIBOR)

The Nigerian money market reference rate, the NIBOR, recorded mild fluctuations on all tenors. The rates moved in tandem with developments at the interbank market. The weighted average 30-day NIBOR rose from 17.90 per cent in July to peak at 39.24 per cent in October. It, thereafter, fell to 20.02 and 16.32 per cent in November and December 2017, respectively. The average 30-day NIBOR rate declined to 23.16 per cent in the second half of 2017, from 27.83 per cent in the preceding half year, implying that liquidity conditions eased (Table 5.1).

5.2 Foreign Exchange Market

During the second half of 2017, the Bank continued its foreign exchange interventions to provide liquidity in the market, ease demand pressures and stabilize the exchange rate. Activities at the newly introduced Investors' and Exporters' window helped to support foreign exchange liquidity for willing buyers and sellers, thereby absorbing speculative pressures in the market. Complementary reforms and interventions during the period aimed at encouraging capital inflows to further improve foreign exchange liquidity. The reforms were the intensification of the policy on repatriation of export proceeds and return of unutilized foreign exchange sourced from CBN auctions. The Bank also sustained the implementation of existing measures including the restriction of access to foreign exchange for 41 items, the use of Bank Verification Numbers (BVN) in BDC transactions, resumption of sale of foreign exchange by the Bank and International Money Transfer Operators (IMTOs) to BDCs, as well as special foreign exchange auction to targeted sectors, amongst others. Consequently, the rates at the Bureau-de-Change (BDC) and Nigeria Autonomous Foreign Exchange (NAFEX) segments moved towards convergence, indicating the narrowing of arbitrage opportunities in the market. In addition, the average naira exchange rate at the inter-bank segment of the foreign exchange market remained stable.

Figure 5.4
Daily Naira/US Dollar Exchange Rate (January - December 2017)



5.2.1 Average Exchange Rates

The interbank exchange rate depreciated slightly by 0.06 per cent, from an average of ₦305.71/US$ in the first half of 2017 to ₦305.89/US$ in the second half. The BDC rate, however, appreciated by 17.27 per cent from an average of ₦426.85/US$ to ₦363.99/US$ over the same period (Table 5.2).

Table 5.2
Average Monthly Spot Exchange Rates (January 2017 – December 2017) (N/US$)

Period	Interbank Rate	BDC Rate
2017: Jan	305.20	493.29
Feb	305.31	494.70
Mar	306.40	429.48
Apr	306.05	392.89
May	305.54	384.48
Jun	305.72	366.25
Average	**305.70**	**426.85**
2017: Jul	305.72	365.38
Aug	305.86	365.57
Sep	305.67	365.55
Oct	305.89	362.21
Nov	305.90	362.40
Dec	306.31	362.83
Average	**305.89**	**363.99**

5.2.2 End-Period (Month) Exchange Rates

The end-period analysis showed that at the interbank foreign exchange segment, the naira depreciated by 0.04 per cent to ₦305.84/US$ at end-December from ₦305.71/US$ at end-June, 2017. At the BDC segment, the Naira, however, appreciated by 13.11 per cent to ₦363.08/US$ from ₦410.67/US$ over the same period (Figure 5.5 and Table 5.3). The difference between the average and end-period exchange rates in the BDC segment showed that demand pressure moderated towards the end of the year.

Table 5.3
End-Month Exchange Rates (January 2017 – December 2017) (N/US$)

Month/Year	Interbank Rate	BDC 'B' Rate
2017H1: Jan	305.25	497
Feb	305.5	450
Mar	306.35	385
Apr	305.85	390
May	305.4	376
Jun	305.9	366
Average	**305.71**	**410.67**
2017H2: Jul	305.65	362
Aug	305.85	364
Sep	305.75	364.5
Oct	305.8	362
Nov	306	363
Dec	306	363
Average	**305.84**	**363.08**

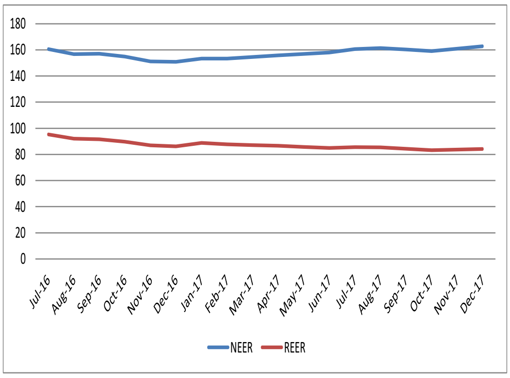
5.2.3 Nominal and Real Effective Exchange Rates

The Nominal Effective Exchange Rate (NEER) depreciated by 3.84 per cent to an average of 160.83 in the second half of 2017 from 155.31 in the first half. It also depreciated by 3.49 per cent when compared with the corresponding period of 2016. On the other hand, the Real Effective Exchange Rate (REER) appreciated by 2.82 per cent from an average of 86.79 in the first half of 2017 to 84.41 in the second half, indicating improvements in trade competitiveness for Nigeria. When compared with the corresponding period of 2016, the average REER also appreciated by 7.00 per cent (Table 5.4).

Table 5.4
Nominal and Real Effective Exchange Rates Indices (2016H2-2017H2)

DATE	NEER	REER
Jul-16	160.52	95.33
Aug-16	156.75	92.08
Sep-16	157.06	91.57
Oct-16	154.88	89.78
Nov-16	151.21	87.02
Dec-16	150.87	86.16
2016: H2 Average	**155.22**	**90.32**
Jan-17	153.29	88.75
Feb-17	153.33	87.71
Mar-17	154.54	87.03
Apr-17	155.84	86.62
May-17	156.95	85.71
Jun-17	157.92	84.94
2017: H1 Average	**155.31**	**86.79**
Jul-17	160.61	85.55
Aug-17	161.37	85.41
Sep-17	160.32	84.32
Oct-17	159.05	83.21
Nov-17	160.9	83.72
Dec-17	162.74	84.24
2017: H2 Average	**160.83**	**84.41**

Figure: 5.5
Nominal and Real Effective Exchange Rates Indices (July 2016 – December 2017)



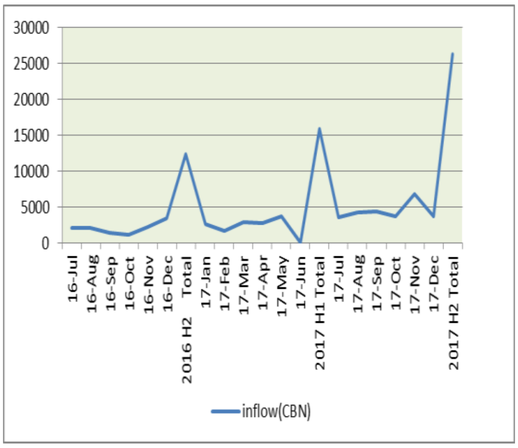
5.2.5 Foreign Exchange Flows through the CBN

Foreign exchange inflows through the CBN increased by 65.29 per cent to US$26,337.00 million in the second half of 2017, from US$15,933.36 million in the first half. It also increased by 113.20 per cent when compared with US$12,353.03 million in the corresponding period of 2016. Similarly, the foreign exchange outflows through the CBN increased by 42.66 per cent to US$18,197.65 million in the second half, from US$12,755.61 million in the first half. When compared with US$12,421.32 million in the corresponding period of 2016, it increased by 46.50 cent. Thus, in the review period, there was a higher net inflow of US$8,139.35 million compared with US$5,908.87 million in the first half. This was in contrast to the net outflow of US$474.99 million in the corresponding half of 2016 (Table 5.5 and Figure 5.7). The increased net inflow was traceable to improved oil receipts and accretion to external reserves.

Table 5.5
Monthly Foreign Exchange Flows through the CBN (January 2016 – Dec 2017)

Dates	Inflow (CBN)	Total Outflow (CBN)	Net Flow (CBN)
16-Jan	1329.40	1687.59	-358.19
16-Feb	1221.53	1025.73	195.80
16-Mar	1611.38	1764.89	-1918.40
16-Apr	900.51	2053.33	-1152.80
16-May	1779.42	1690.29	89.13
16-Jun	1870.88	2521.03	-650.15
2016 H1 Total	**8713.12**	**10742.86**	**-2029.70**
16-Jul	2126.36	2671.08	-544.72
16-Aug	2112.69	2430.51	-317.82
16-Sep	1379.97	2669.87	-1289.90
16-Oct	1096.83	2119.19	-1022.30
16-Nov	2251.90	1061.94	783.17
16-Dec	3385.31	1468.73	1916.58
2016 H2 Total	**12353.03**	**12421.32**	**-474.99**
17-Jan	2605.50	1055.84	1549.66
17-Feb	2374.48	978.56	1395.92
17-Mar	1693.40	1672.59	20.81
17-Apr	2874.86	2164.39	710.47
17-May	2712.38	3676.12	-954.74
17-Jun	3672.74	3208.11	3186.75
2017 H1 Total	**15933.36**	**12755.61**	**5908.87**
17-Jul	3615.10	3358.32	256.78
17-Aug	4211.75	3594.33	617.42
17-Sep	4328.97	2390.41	1938.56
17-Oct	3688.39	2891.97	796.42
17-Nov	6811.96	2957.60	3854.36
17-Dec	3680.83	3005.02	675.81
2017 H2 Total	**26337.00**	**18197.65**	**8139.35**

Figure 5.6
Monthly Foreign Exchange Flows through the CBN (Jul 2017 – Dec 2017)



5.2.6 Foreign Exchange Flow through the Economy

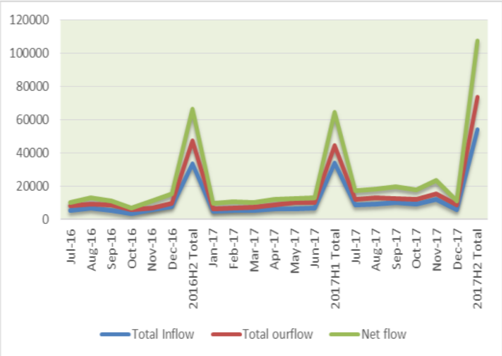
Gross foreign exchange inflow to the economy increased by 58.32 per cent to US$53,650.70 million in the second half, from US$33,886.85 million in the first half of 2017. It also increased by 59.70 per cent when compared with

US$33,594.00 million in the corresponding period of 2016. Similarly, gross foreign exchange outflow increased by 88.59 per cent to US$19,799.77 million in the second half of 2017, from US$10.498.63 million in the first half. When compared with US$13,673.02 million in the corresponding period of 2016, it increased by 44.81 per cent. Thus, during the second half of 2017, total foreign exchange flows through the economy resulted in a higher net inflow of US$33, 850.93 million compared with US$20,027.22 million and US$19,120.98 million in the first half and the corresponding period of 2016, respectively. This represented increases of 69.02 and 77.04 per cent relative to the first half of 2017, and the corresponding period of 2016, respectively. The increased net inflow through the economy during the period reflected increased foreign exchange receipts from the recovery of crude oil prices as well as improved autonomous inflows.

Table 5.6
Monthly Foreign Exchange Flows through the Economy
(Jan 2016 – Dec 2017) (US$ Million)

Date	Inflow(CBN)	Inflow(Auto)	Total Inflow	Outflow(CBN)	Outflow(Auto)	Totaloutflow	Netflow	Netflow(CBN)	Netflow(Auto)
Jan-16	1329.4	4078.86	5408.26	1687.59	235.72	1923.31	3202.97	-358.19	3843.14
Feb-16	1221.53	3096.19	4317.72	1025.73	189.61	1215.34	3104.18	195.8	2906.58
Mar-16	1611.38	3669.51	5280.77	1764.89	187.71	1952.6	3100.02	-153.51	3481.8
Apr-16	900.51	3209.39	4351.88	2053.33	135.74	2265.41	2086.47	-1152.82	3073.65
May-16	1779.42	2555.46	4334.88	1690.29	178.35	1868.64	2162.55	89.13	2377.11
Jun-16	1870.88	3835.47	5706.35	2521.03	210.6	2310.43	2974.72	-650.14	3624.87
2016H1 Total	**8,713.12**	**20,444.88**	**29,158.00**	**10,742.86**	**1,137.23**	**9,605.63**	**16,630.91**	**- 2,676.24**	**19,307.15**
Jul-16	2126.36	2913.56	5039.92	2671.08	177.25	2848.33	2191.59	-544.72	2736.31
Aug-16	2112.69	4420.69	6533.38	3430.54	118.26	2548.8	3984.58	-317.82	4302.43
Sep-16	1379.97	4115.34	5495.31	2669.87	299.53	2969.4	2525.91	-1289.9	3815.81
Oct-16	1096.83	2277.93	3374.76	2119.19	130.19	2249.38	1125.38	-1022.9	2147.74
Nov-16	2251.9	3306.69	5558.59	1061.94	194.96	1256.9	4301.69	1189.96	3111.73
Dec-16	3385.31	4206.73	7592.04	1468.73	331.48	1800.21	5791.83	1916.58	3875.25
2016H2 Total	**12,353.06**	**21,240.94**	**33,594.00**	**12,421.35**	**1,251.67**	**13,673.02**	**19,120.98**	**- 68.80**	**19,989.27**
Jan-17	2605.5	2142.96	4748.46	1055.84	179.12	1234.96	3513.5	1549.66	1963.83
Feb-17	2374.48	2935.28	5309.76	978.56	224.32	1202.88	4106.88	1395.92	1963.83
Mar-17	1693.4	3345	5038.4	1672.59	255.2	1927.79	3110.52	20.81	3089.8
Apr-17	2874.86	3203.72	6078.58	2164.39	129.9	2294.29	3784.29	710.47	3073.82
May-17	2712.38	3543.22	6255.6	3676.12	162.59	3838.71	2416.89	963.74	3380.63
Jun-17	3672.74	2783.31	6456.05	3208.11	152.8	3360.91	3095.14	464.63	2630.51
2017H1 Total	**15,933.36**	**17,953.49**	**33,886.85**	**12,755.61**	**1,103.93**	**10,498.63**	**20,027.22**	**5,105.23**	**16,102.42**
Jul-17	3867.04	4689.85	8556.89	3358.32	250.35	3608.67	4948.22	508.72	4448.5
Aug-17	4211.75	4896.53	9108.28	3594.33	196.61	3790.94	5317.34	617.42	4699.92
Sep-17	4328.97	5467.56	9796.53	2390.41	379.23	2769.64	7026.89	1938.56	5088.33
Oct-17	3688.39	5168.63	8857.02	2891.97	229.12	3121.09	5735.93	796.42	4939.51
Nov-17	6811.96	4986.71	11798.67	2957.6	546.82	3504.42	8294.25	3854.36	4439.89
Dec-17	3680.83	1852.48	5533.31	2584.46	420.55	3005.01	2528.3	1096.37	1431.93
2017H2 Total	**26,588.94**	**27,061.76**	**53,650.70**	**17,777.09**	**2,022.68**	**19,799.77**	**33,850.93**	**8,811.85**	**25,048.08**

Figure 5.7
Monthly Foreign Exchange Flows through the Economy (Jul 2017 – Dec 2017) (US$ Million)



5.3 Capital Market

Activities in the Nigerian capital market in the second half of 2017 were mainly bullish, reflecting positive investor sentiments attributable to generally improving macroeconomic conditions. In particular, the growing external reserves, stable exchange rate and moderating inflation, on the back of rising crude oil prices, helped to boost investor confidence in the economy. Also, the sustained tight monetary policy stance of the Bank improved returns on domestic assets and attracted foreign inflows into the capital market. The continued BREXIT uncertainty, generally accommodative monetary policy stance in the advanced economies, helped to support the flow of foreign capital in search of yields in the emerging markets including Nigeria.

5.3.1 Equities Market

The All-Share Index (ASI) increased by 15.48 per cent to 38,243.19 at end-December 2017 from 33,117.48 at end-June 2017. It, similarly, increased by 42.30 per cent compared with 26,874.62 at end-December 2016. Market capitalization (MC) increased by 18.86 per cent to ₦13.61 trillion at end-December 2017, from ₦11.45 trillion at end-June 2017. Also, when compared with ₦9.25 trillion at end-December 2016, it increased by 47.14 per cent. The year-on-year increase of 42.30 per cent in the ASI was driven mainly by strong performance in the food & beverage and banking sectors, which increased by 13.65 and 19.10 per cent, respectively, above their levels at end-December 2016.

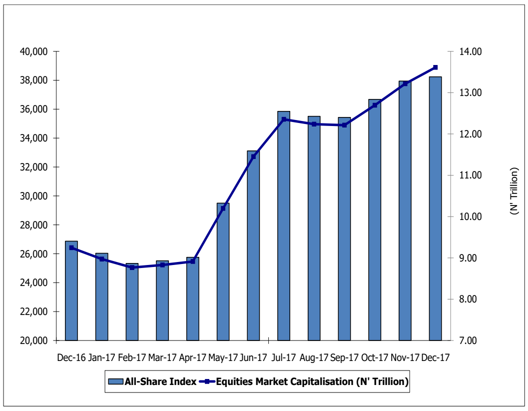
Table 5.7
NSE All-Share Index (ASI) and Market Capitalization (MC) (December 2016 – December 2017)

Date	ASI	MC(Equities) N'Trillion)
Dec-16	26,874.62	9.25
Jan-17	26,036.24	8.97
Feb-17	25,329.08	8.77
Mar-17	25,516.34	8.83
Apr-17	25,758.51	8.91
May-17	29,498.31	10.20
Jun-17	33,117.48	11.45
Jul-17	35,847.75	12.35
Aug-17	35,504.62	12.24

Sep-17	35,429.31	12.21
Oct-17	36,680.29	12.69
Nov-17	37,944.60	13.21
Dec-17	38,243.19	13.61

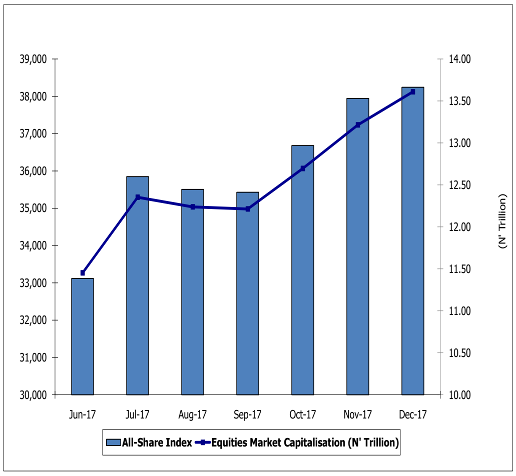
Source: NSE

Figure 5.8
NSE ASI and MC (December 2016– December 2017)



Source: NSE

Figure 5.9
NSE ASI and MC (June 2017 – December 2017)



Source: NSE

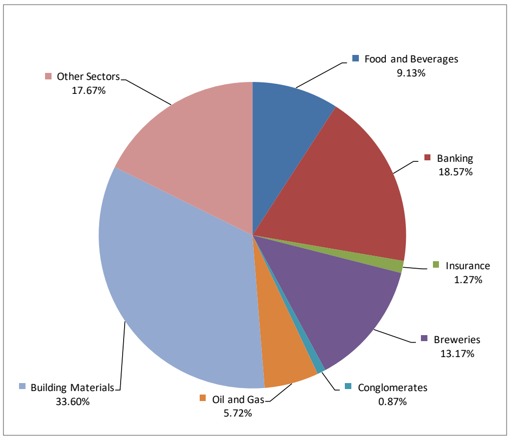
5.3.2 Market Turnover

Aggregate stock market turnover in the second half of 2017 increased by 34.49 per cent to 59.39 billion shares, valued at ₦803.82 billion in 491,300 deals compared with 44.16 billion shares, valued at ₦467.67 billion in 448,950 deals in the first half of 2017. On a year-on-year basis market turnover increased by 75.50 per cent from 33.84 billion shares, valued at ₦263.50 billion in 380,997 deals. Foreign portfolio investment inflow exceeded outflow by ₦194.85 billion in the second half of 2017, indicating sustained investor confidence in the economy.

5.3.3 Sectoral Contribution to Equity Market Capitalization

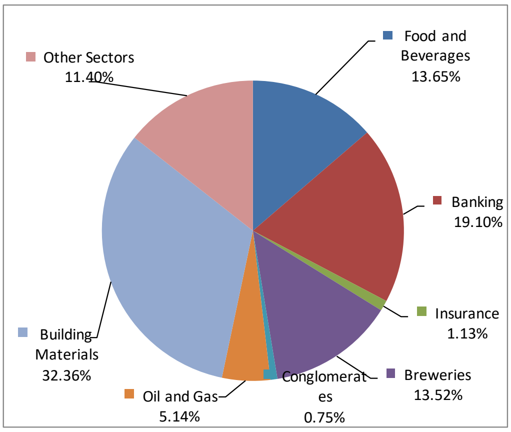
The construction sector still dominated overall market capitalization and was primarily driven by activities in the building materials sub-sector. The contribution of the building materials sub-sector, however, declined to 32.36 per cent at end-December 2017 from 33.60 per cent in the preceding half year. The dominance of the building materials sub-sector was largely attributable to the share of Dangote cement in the market. Other major sub-sectors were banking, food & beverages and breweries, with market shares of 19.10, 13.65 and 13.52 per cent, respectively, at end-December 2017 (Figure 5.12).

Figure 5.10
NSE Market Capitalisation by Sector as at End-June 2017



Source: NSE

Figure 5.11
NSE Market Capitalisation by Sector as at End-December 2017

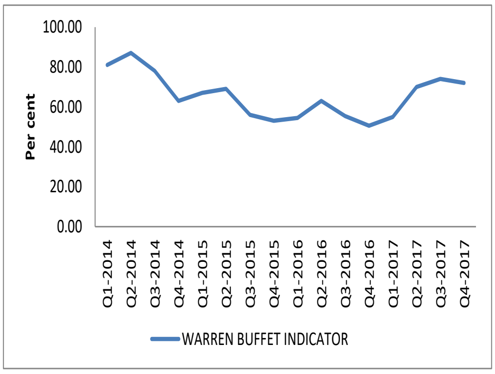


Source: NSE

5.3.4 The Warren Buffett Valuation Metric and Nigeria's Equities Market

The analysis of Warren Buffett valuation metric showed that the Nigerian equities market was under-valued. At 74.0 per cent in the third quarter and 72.0 per cent in the fourth quarter of 2017, the metric was below the threshold of 75.0 - 115.0 per cent. The development was attributable to the following: still fragile economic recovery, weak corporate earnings and the ongoing normalization of the US monetary policy resulting in more attractive yields. The undervaluation of equities present attractive investment opportunities for domestic and foreign investors, further strengthened by improving economic conditions and rising crude oil prices.

Figure 5.12
Warren Buffett Valuation of Nigerian Equities Market



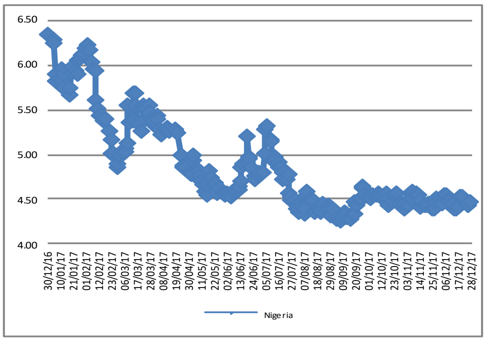
5.3.5 Bond Market

Activities in the bonds market were dominated by Federal Government of Nigeria (FGN) securities in the second half of 2017. There was also some activity in the Sub-national government and corporate bonds segments, with the latter recording the least share by market volume.

5.3.5.1 FGN Eurobond

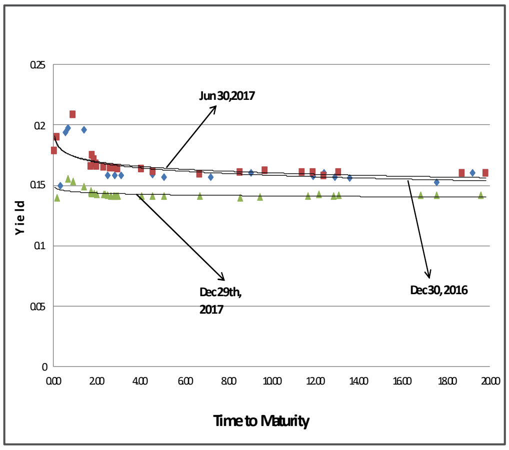
The 10-year dollar-denominated bond yields for Nigeria decreased by 33 basis points to 4.47 per cent at end-December 2017, from 4.80 per cent at end-June 2017. When compared with 6.35 per cent at end-December 2016, it decreased by 188 basis points (Figure 5.14). The development was attributable to improved perception by investors of the country's sovereign risk.

Figure 5.13
10-Year U.S. Dollar-denominated Bond Yield for Nigeria (Dec 31, 2016 – Dec 29, 2017)



FGN bond yields fell by 37 basis points to 16.37 per cent in December 2017 when compared with 16.74 per cent at end-June, 2017 and 3 basis points when compared with 16.40 per cent at end-December 2016. The observed negative slope suggests that there is perceived uncertainties about economic conditions in the longer-term and investors are more optimistic about the current economic conditions (Figure 5.15).

Figure 5.14
FGN Bonds Yield Curves: end-Dec. 2016 vs. end-Jun. 2017 vs. end-Dec. 2017



5.3.5.2 State/Local Government Bonds

The sub-national bonds market continued to witness low activity during the review period. The total value of outstanding state/local governments bonds declined by 0.13 per cent to ₦562.81 billion at end-December 2017 from ₦563.58 billion at end-June 2017. When compared with ₦516.58 billion at end-December 2016, it, however, increased by 1.98 per cent.

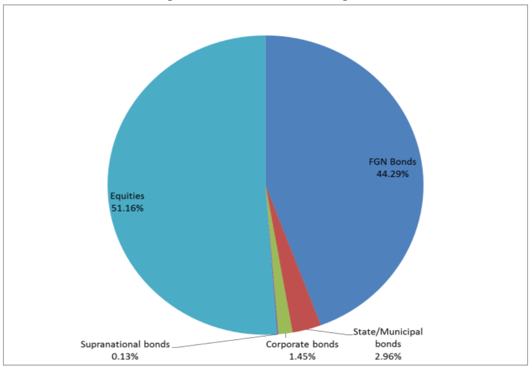
5.3.5.3 Corporate Bonds

Activity in the corporate bonds segment declined during the review period. The value of outstanding corporate bonds at end-December 2017, declined by 7.04 and 1.94 per cent to ₦276.50 billion from ₦297.44 billion and ₦281.97 billion in the first half of 2017 and the corresponding period of 2016, respectively. The development was traceable to increased activities in the sovereign bond market.

5.3.5.4 Overall Analysis of the Nigerian Capital Market

The value of FGN bonds increased significantly by 26.39 per cent to ₦8.43 trillion at end-December 2017 from ₦6.67 trillion at end-June 2017, and by 38.20 per cent when compared with ₦6.10 trillion at end-December 2016. FGN bonds accounted for 44.29 per cent of aggregate market capitalization as at end-December 2017. The value of state/municipal bonds, corporate bonds and supranational bonds were N562.58 billion, N276.50 billion and N24.95 billion, accounting for 2.96, 1.45 and 0.13 per cent of aggregate market capitalization, respectively. The equities market contributed 51.16 per cent of aggregate market capitalization at end-December 2017, while FGN bonds, state/municipal bonds, corporate bonds and supranational bonds accounted for the balance of 48.84 per cent (Figure 5.16).

Figure 5.15
Structure of the Nigerian Capital Market (December, 2017)



5.4 Global Financial Market Developments

During the review period, global financial markets remained moderately calm, although uncertainties following developments in important long-standing trade agreements, weighed on financial market sentiments and global investments. In particular, the current NAFTA renegotiations and BREXIT discussions, heightened trade barriers and regulatory realignments, and were compounded by geopolitical tensions on the Korean peninsula and the Middle East. The heightened risks were reflected in the growing share of companies with low investment grade ratings in advanced economy bond markets. Generally, the environment of continuing monetary accommodation to revive global economic activity and inflation, led to rising asset valuations and higher leverage, with the search for yields shifting sharply into the nonbank sector. Consequently, financial stability risks were spilling over from the banking system to the nonbank and market sectors. Also, unconventional monetary policies have forced substantial portfolio adjustments in the private sector and across borders, making financial market vulnerability less predictable than in previous cycles. Nonetheless, the key challenge confronting policy makers was to guard against the build-up of financial vulnerabilities, while ensuring that monetary policy remained supportive of global recovery.

Following these developments, most currencies appreciated against the US dollar, as oil and other commodity prices continued to improve, although the US dollar rallied in November 2017. As a result, the performance of major global stock markets remained generally positive.

5.4.1 Money Market and Central Bank Policy Rates

Liquidity conditions were largely influenced by moderating risks in the global financial markets, resulting from the generally improving macroeconomic environment. In the advanced economies, particularly in the US and the UK, the earlier trend of low inflation has been progressively reversed, leading to continued normalization of monetary policy, while in the EU and Japan, inflation has remained muted. In the emerging markets and developing economies, the reversal in currency depreciation following improvements in oil and other commodity prices, gave room for downward policy rate adjustments to accommodate growth concerns. Headwinds to the stability in the global macroeconomic environment, however, remained the uncertainties surrounding BREXIT negotiations, direction of US trade policy, sustainability of improving oil and other commodity prices. Accordingly, the US and the UK raised their policy rates to improve yields on domestic assets and contain inflationary pressures, while the EU and Japan retained their rates in the review period. Amongst the emerging market and developing economies, Brazil, Russia, Ghana and Indonesia lowered their policy rates to accommodate growth concerns as inflationary pressures moderated, while China, South Africa, Kenya and Nigeria maintained their policy rates.

Table 5.8
Policy Rates of Selected Countries June – December 2017

Country	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17
Kenya	10.00	10.00	10.00	10.00	10.00	10.00	10.00
S. Africa	6.75	6.75	6.75	6.75	6.75	6.75	6.75
Ghana	22.50	21.00	21.00	21.00	21.00	20.00	20.00
Nigeria	14.00	14.00	14.00	14.00	14.00	14.00	14.00
Brazil	10.25	9.25	8.25	8.25	7.50	7.50	7.50
USA	1.00-1.25	1.00-1.25	1.00-1.25	1.00-1.25	1.00-1.25	1.00-1.25	1.25-1.50
Japan	0.00-0.10	0.00-0.10	0.00-0.10	0.00-0.10	0.00-0.10	0.00-0.10	0.00-0.10
Euro Area	0.00	0.00	0.00	0.00	0.00	0.00	0.00
India	6.25	6.25	6.00	6.00	6.00	6.00	6.00
Russia	9.25	9.00	9.00	8.50	8.50	8.25	7.75
China	4.35	4.35	4.35	4.35	4.35	4.35	4.35
UK	0.25	0.25	0.25	0.25	0.25	0.50	0.50
Indonesia	4.75	4.50	4.50	4.25	4.25	4.25	4.25

5.4.2 Capital Market

The performance of major global stock markets remained generally positive in the review period. In Europe, the UK FTSE 100, French CAC 40, German DAX and Russian MICEX indices increased by 5.13, 3.75, 4.81 and 12.25 per cent, respectively. In North America, the United States S&P 500 and Canadian S&P/TSX Composite indices increased by 10.32 and 6.76 per cent, respectively, while the Mexican Bolsa decreased by 1.01 per cent. In South America, the Brazilian Bovespa, Argentine Merval and the Columbia COLCAP indices increased by 21.47, 37.21 and 3.47 per cent, respectively. In Asia, the Japanese Nikkei 225, Chinese Shanghai SE and Indian BSE Sensex indices increased by 13.63, 3.59 and 10.14 per cent, respectively. In Africa, the Nigerian NSE All-Share, South African JSE All-Share, Kenyan Nairobi NSE 20, Egyptian EGX CASE 30 and Ghanaian GSE All Share indices increased by 15.48, 15.29, 2.90, 11.36 and 31.31 per cent, respectively.

Table 5.9
Selected International Stock Market Indices as at December 29, 2017

Country	Index	30-Dec-16	30-Jun-17	29-Dec-17	December 30, 2016-December 29, 2017 % Change	Jun 30 - Dec 29, 2017 % Change
AFRICA						
Nigeria	ASI	26,874.62	33,117.48	38,243.19	42.30	15.48
South Africa	JSE African AS	50,653.54	51,611.01	59,504.67	17.47	15.29
Kenya	Nairobi NSE 20	3,186.21	3,607.18	3,711.94	16.50	2.90
Egypt	EGX CSE 30	12,290.61	13,487.36	15,019.14	22.20	11.36
Ghana	GSE All Share	1,689.18	1,964.55	2,579.72	52.72	31.31
NORTH AMERICA						
US	S&P 500	2,238.83	2,423.41	2,673.61	19.42	10.32
Canada	S&P/TSX Composite	15,287.59	15,182.19	16,209.13	6.03	6.76
Mexico	Mexico Bolsa (IPC)	45,642.90	49,857.49	49,354.42	8.13	-1.01
SOUTH AMERICA						
Brazil	Bovespa Stock	60,227.29	62,899.97	76,402.08	26.86	21.47
Argentina	Merval	16,917.86	21,912.63	30,065.61	77.72	37.21
Colombia	COLCAP	1,351.68	1,462.90	1,513.65	11.98	3.47
EUROPE						
UK	FTSE 100	7,142.83	7,312.72	7,687.77	7.63	5.13
France	CAC 40	4,862.31	5,120.68	5,312.56	9.26	3.75
Germany	DAX	11,481.06	12,325.12	12,917.64	12.51	4.81
Russia	MICEX	2,232.72	1,879.50	2,109.74	-5.51	12.25
ASIA						
Japan	NIKKEI 225	19,114.37	20,033.43	22,764.94	19.10	13.63
China	Shanghai SE A	3,249.59	3,343.39	3,463.48	6.58	3.59
India	BSE Sensex	26,626.46	30,921.61	34,056.83	27.91	10.14

Source: Bloomberg

5.4.3 Commodities

As in the first half of 2017, commodity prices continued their recovery in the second half. The recovery was witnessed in both fuel and non-fuel commodity prices. Energy price index as shown by the price of the Organization of the Petroleum Exporting Countries (OPEC) reference crude oil basket, rose from an average of US$49.95pb in the first half to US$56.43pb in the second half of 2017. Crude oil prices were still supported by the extension of the agreement between OPEC and non-OPEC producers including Russia to freeze output. Non-fuel price index, as reflected in the behaviour of metal prices, also increased during the review period. In particular, the prices of Aluminum and Zinc[1] rose from US$1,907/mt and US$2,593/mt in the first half to US$2,103/mt and US$3,230/mt in the second half of 2017, respectively. The development was largely due to improvements in global growth prospects and the strengthening of aggregate demand. The increase in metal prices was occasioned by improving macroeconomic outcomes from China following the rebalancing programme.

[1] World Bank Commodities Price Data (The Pink Sheet) @www.worldbank.org/commodities

The Food and Agriculture Organization (FAO) Food Price Index, however, fell by 3.54 per cent from 175.3 points in June to 169.1 points in December 2017. During the review period, the sub-indices of meat, cereals and dairy fell, while that of vegetable oil and sugar increased. The development was due to strong supply of meat, ample supplies of cereals, particularly maize in South America and the Northern Hemisphere, as well as high export supplies of dairy and weak demand.

5.4.4 Foreign Exchange Market

During the second half of 2017, most currencies appreciated against the US dollar, as oil and other commodity prices continued to improve and earlier expectations of an expansionary US fiscal policy diminished. Although the US dollar rallied in November 2017 against the backdrop of continued monetary policy normalization, high expectations of a positive outcome on the North American Free Trade Agreement (NAFTA) negotiations and promise of a substantial corporate tax cut, economic agents remained cautious on the ability of the administration to deliver on these expectations. Accordingly, in North America, the Canadian dollar appreciated by 3.13 per cent while the Mexican peso depreciated against the U.S. dollar by

7.83 per cent. In South America, the Brazilian real and the Argentine peso depreciated against the U.S. dollar by 0.04 and 10.71 per cent, respectively, while the Colombian peso appreciated against the U.S dollar by 1.88 per cent in the period under review.

In Europe, the Pound Sterling, the euro and the Russian ruble appreciated against the U.S dollar by 3.72, 5.07 and 2.29 per cent, respectively. In Asia, the Japanese yen depreciated against the U.S dollar by 0.27 per cent, while the Chinese yuan and the Indian rupee both appreciated against the U.S. dollar by 4.09 and 1.11 per cent, respectively.

In Africa, the Nigerian naira and Ghanaian cedi depreciated against the U.S dollar by 0.03 and 2.11per cent, respectively, while the South African rand, Kenyan shilling and the Egyptian pound appreciated against the U.S. dollar by 5.59, 0.55 and 1.78 per cent, respectively.

Table 5.10
Exchange Rates of Selected Countries (value in currency units to US$)

Exchange Rates of Selected Countries (Value in currency units to US$)						
	Currency	**30-Dec-16**	**30-Jun-17**	**29-Dec-17**	**Jun 17 - Dec. 17 (% App/Dep)**	**Dec 16 - Dec 17 (% App/Dep)**
AFRICA						
Nigeria	Naira	305.00	305.90	306.00	-0.03	-0.33
South Africa	Rand	13.74	13.07	12.38	5.59	10.96
Kenya	Shilling	102.51	103.75	103.18	0.55	-0.65
Egypt	Pound	18.14	18.13	17.81	1.78	1.86
Ghana	Cedi	4.24	4.41	4.51	-2.11	-5.88
NORTH AMERICA						
Canada	Dollar	1.34	1.30	1.26	3.13	6.59
Mexico	Peso	20.73	18.12	19.66	-7.83	5.45
SOUTH AMERICA						
Brazil	Real	3.26	3.31	3.31	-0.04	-1.47
Argentina	Peso	15.88	16.63	18.62	-10.71	-14.73
Colombia	Peso	3002.00	3043.11	2986.84	1.88	0.51
EUROPE						
UK	Pound	0.81	0.77	0.74	3.72	9.43
Euro Area	Euro	0.95	0.88	0.83	5.07	14.05
Russia	Ruble	61.54	58.94	57.63	2.29	6.79
ASIA						
Japan	Yen	116.96	112.39	112.69	-0.27	3.79
China	Yuan	6.95	6.78	6.51	4.09	6.69
India	Rupee	67.92	64.58	63.87	1.11	6.34
Source: bloomberg						

Green Bond and Infrastructural Development in Nigeria

The imperative to safeguard the sustainability of economic development strategies is driving the search for policy alternatives and viable, environmentally-conscious instruments of economic management. The latest initiative in this regard is the issuance of green bonds. The World Bank describes a green bond as a debt security, issued to raise capital and specifically to enhance environmental sustainability by supporting climate-related or environmental projects. The distinguishing feature of the green bond from other debt securities is the utilization of accrued funds for a specific pre-determined project, enabling investors to assess the actual environmental impact of the project to be funded with the proceeds of the bond.

Globally, several multilateral institutions have issued green bonds. The European Investment Bank (EIB), in 2007 issued a €600 million Climate Awareness Bond that focused on renewable energy and energy efficiency. Instead of a fixed coupon, the bond returns were linked to an equity index. The World Bank, through the International Bank for Reconstruction and Development (IBRD), launched the first labeled "green bond" in 2008 in the sum of SKr 3.35 billion (approximately US$440 million).

The World Bank issuance of the first green bond was aimed at:
Responding to calls from Scandinavian pension funds seeking to support climate-focused projects with a simple fixed-income product, and in line with IBRD's efforts to cater for investors interested in sustainable and responsible investing (SRI); and raising investor and the financial sector awareness on the commitment of developing countries to take decisive actions to combat climate change;

The bond issuance was in line with the World Bank's effort to seek innovative ways to finance climate related projects. By 2015, the IBRD had issued green bonds valued at US$8.5 billion in over 100 transactions in 18 currencies, supporting about 70 climate mitigation and adaptation projects across several countries in the developing world (World Bank, 2015).

Other notable multilateral institutions involved in the issuance of green bonds include the African Development Bank (AfDB) and the International Finance Corporation (IFC). The African Development Bank had issued a total of US$500 million worth of green bonds in October 2013, while the International Finance

Corporation (IFC), a subsidiary of the World Bank Group, issued over 37 green bonds, raising US$3.8 billion in nine currencies, in the same year. Generally, four broad steps are followed in issuing green bonds. These are:

Defining Project Selection Criteria

At this initial stage the issuer defines the type of 'green' project for which it is seeking the green bonds. The ultimate aim being to support a project anticipated to translate into low carbon emissions to the environment and climate-resilient growth.

Establishing Project Selection Process

This entails a rigorous project review and approval process, which includes; preliminary screening, identifying and managing potential environmental and/or social impacts, and obtaining the approval of the project promoters.

Earmarking and Allocating Proceeds

The issuer discloses how it will separate green bond proceeds and make periodic allocations to eligible investors. Funds are periodically allocated in a ratio equal to the disbursements of eligible projects.

Monitoring and Reporting

The issuer monitors the implementation of the green projects and provides periodic reports detailing the utilization of proceeds and the expected environmental sustainability impacts.

Project implementation and monitoring follows the Green Bond Principle (GBP) which aims to encourage disclosure, thereby enhancing transparency and integrity in the development of the green bond market.

The GBP have core components: Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds, and Reporting.

There are four basic types of green bonds, namely:

Standard Green Use of Proceeds Bond: A standard recourse-to-the-issuer debt obligation aligned with the GBP;

<u>Green Revenue Bond</u>: A non-recourse-to-the-issuer debt obligation aligned with the GBP in which the credit exposure in the bond is to the pledged cash flows of the revenue streams, fees, and/or taxes, and whose use of proceeds go to related or unrelated Green Project(s);

<u>Green Project Bond</u>: A project bond for a single or multiple Green Project(s) for which the investor has direct exposure to the risk of the project(s) with or without potential recourse to the issuer, and which are aligned with the GBP; and

<u>Green Securitised Bond</u>: A bond collateralised by one or more specific Green Project(s), including but not limited to covered bonds, ABS, MBS, and other structures; and aligned with the GBP. The first source of repayment is generally the asset cash flows. These type of bonds cover, for example, asset-backed securitization of rooftop solar PV and/or energy efficiency assets;

The GBP recognizes several categories of potential eligible projects, including, but not limited to the following:

<u>Renewable Energy Projects</u>; Enhancing energy efficiency (including efficient buildings), sustainable waste management, sustainable land use (including sustainable forestry and agriculture), biodiversity conservation, clean transportation, sustainable water management (including clean potable drinking water), and climate change adaptation.

The Green Bond market grew from approximately US$4 billion in 2010 to over US$37 billion in 2014, with corporations like Toyota and public entities such as the State of Massachusetts having issued over half of the total value.

In September 2016, the Nigerian President, Muhammadu Buhari, signed the Paris Agreement on Climate Change, joining other nations to commit to reversing the negative effects of climate change. Under the Paris Agreement, each country was required to clearly specify efforts to be undertaken to achieve the objectives of the agreement. These commitments, made on a country-by-country basis are referred to as Nationally Determined Contributions (NDCs). Nigeria has committed to reducing carbon emissions by 20 per cent unconditionally, and 45 per cent; with international support, by 2030 through environmentally efficient energy, transport and agriculture projects. Such projects are anticipated to reduce carbon emissions and mitigate the effects of climate change including desertification, flooding, erosion, erratic rainfall, and other climate change-induced events. Achieving the NDCs requires the implementation of various projects in different sectors of the economy which would require adequate financing. Consequently, the Federal Government of Nigeria issued its first green bond totaling ₦10.69 billion in December, 2017 for a 5-year tenor at 13.48 per cent. The green bond presents a unique opportunity for governments to seek financing for renewable energy and other climate friendly projects to bridge infrastructure deficits where they may exist, and to boost national productivity at a lower cost. This would enable governments attain the twin objectives of fiscal efficiency and environmental sustainability.

The FGN Sovereign Sukuk: Implication for Monetary Policy

The immense financing gaps occasioned by the decline in oil revenue and binding constraints Nigeria's vast infrastructural deficit poses to economic development has made it imperative for governments at both federal and subnational levels to seek alternative and unconventional financing sources in order to fulfill their development aspirations. One such source which continues to garner attention in recent times is Islamic 'non-interest' finance, a fast growing subsector with assets estimated in excess of US$2.5trillion. Islamic finance refers to banking or financing activity compliant and guided by the principles of Islamic law (Shariah); and includes 'Sukuk' as one of several products/instruments of Islamic financing. The term "Sukuk" is an Arabic word which simply means "certificates". Technically, Sukuk refers to Islamic bonds structured to generate returns to ethical investors, without infringing on the Islamic injunction which prohibits interest payment or usury. The Security and Exchange Commission (SEC Rules 2013) describes Sukuk as: investment certificates or notes of equal value which evidences proportionate interest and/or ownership of tangible assets, 'usufructs' and services or investment in the assets of particular projects or special investment activity using shariah principles and concepts. While the accrued returns to conventional bond holders signifies the right to receive interest for borrowed monies, Sukuk represents the investors' ownership interest in the underlying asset, business, enterprise or project which entitles them to receive a share of the income generated from trade, transaction or ownership of the asset or business venture.

In November 2017, the Debt Management Office issued, on behalf of the Nigeria Government, the first Sovereign Sukuk Bond at N100 billion, with a seven year tenor.

The bond targeted retail and institutional investors, offering bonds in N1000 denominations, with a minimum subscription amount of 10 units or N10,000.00 and multiples of N1,000.00 thereafter. The bond offered investors a semi-annual, tax-free rental income of 16.47 per annum. The proceeds of the N100 billion Sukuk were earmarked to finance twenty-five (25) Road Projects across the six geopolitical zones of the country.

The Securities and Exchange Commission (SEC) bears responsibility for the oversight and regulation of sovereign, sub-national and corporate Sukuk Bond issuance in Nigeria. This is implemented in line with the framework provided under the Investment and Securities Act 2007 and in accordance to SEC's guidelines on Sukuk. Other institutions including the Central Bank of Nigeria (CBN), Islamic Financial Services Board (IFSB) and the Accounting and Auditing Organisation of Islamic Financial Institutions (AAOIFI) issue guidelines from time to time to streamline the operations of Sukuk.

The selling point of the Sukuk bond, which endeared it to ethical investors, is the low risk profile - as the payment of rental income and the principal at maturity is guaranteed by the full faith and credit of the Federal Government of Nigeria. In addition, the rental income is tax-exempt; and the CBN has conferred liquid asset status on the bond. Accordingly, the Sukuk is listed on the Nigerian Stock Exchange and the FMDQ OTC Securities Exchange, providing avenues for investors wishing to liquidate part or all of their investments prior to maturity. Further, investors may also opt to utilize the bond holdings as collateral for other transactions.

The Sukuk is a veritable innovation in the federal and sub-national governments' quest to diversify funding sources to drive infrastructural and economic development. It is an investment instrument, more suitable to ethical investors who would ordinarily not invest in most pre-existing interest- bearing instruments. The Sukuk thus, provides an avenue to tap into the substantial pool of investible funds at the disposal of ethical investors and prompt their contribution to the development financing needs of the nation in a manner consistent with their investment preferences.

Furthermore, the Sukuk provides an opportunity for ethical and retail investors to participate in the fixed income securities market, thereby encouraging financial inclusion and improving the savings culture and inclusivity of growth in Nigeria. In this regard, the minimum subscription amount for the debut offer was set at ₦10, 000.00 to make it accessible to a wider scope of investors. Accordingly, financial institutions, social and religious organizations, cooperative societies, trust funds and retail investors were expected take advantage of this opportunity.

The Implication of the issuance of the Sovereign Sukuk Bond is the catalytic effect it has had on activating the non-interest bearing segment of the bonds market in Nigeria, thereby further deepening the Nigerian financial market by making additional instruments available to issuers, investors and policy makers.

CHAPTER SIX
ECONOMIC OUTLOOK

6.1 OVERVIEW

In 2017, global output growth further strengthened to 3.7 per cent, up from 3.2 per cent in 2016 (IMF WEO January, 2018). The improvements followed strong growth in world trade supported by a pickup in investments, particularly in the advanced economies, as well as increased manufacturing output in Asia. The development was driven by a number of factors including continued recovery in oil and other commodity prices, occasioned by the extension of the OPEC plus agreement to limit oil production, and geo-political tensions in the Middle East. Other factors included: the expected impact of recent U.S. tax policy adjustments and easier financing conditions particularly in advanced economies. Global growth was, however, moderated by downside risks from inward-looking trade policies, renewed uncertainties associated with the current NAFTA renegotiations.

In the advanced economies, growth was estimated at 2.3 per cent, up from 1.7 per cent in 2016. Growth picked up in most countries of the region, with the United Kingdom being the notable exception. Output growth in the US was 2.3 per cent compared with 1.5 per cent in 2016, due to improved business investment and external demand, reflecting the recovery in the energy sector. In the Euro area and Japan, growth was driven largely by improved private consumption, investment, and external demand. Specifically, output growth in the euro area expanded to 2.4 per cent from 1.8 per cent in 2016. The Japanese economy also expanded at a faster pace by 1.8 per cent compared with 0.9 per cent in 2016. In the United Kingdom, however, growth was projected at 1.7 per cent, down from 1.9 per cent in 2016, partly due to softer growth in private consumption as the depreciation of the pound sterling weakened household real income.

Growth expanded by 4.7 per cent in the Emerging Market and Developing Economies up from 4.4 per cent in the preceding year due to higher domestic demand in China and continued recovery in key economies within the group. China's growth rose marginally to 6.8 per cent from 6.7 per cent in 2016, due to stronger external demand. Output growth in Brazil improved sharply to 1.1 per cent from a contraction of 3.5 per cent in 2016 as a result of strong export performance and diminished pace of contraction in domestic demand. Similarly, output growth in Russia expanded by 1.8 per cent from a contraction of 0.2 per cent in 2016 fuelled by recovering domestic and external demand as well as stabilizing oil prices, easing financial conditions, and improved confidence. Growth in India, however, slowed to 6.7 per cent from 7.1 per cent in 2016, reflecting the lingering impact of the country's currency demonetization exercise coupled with uncertainties related to the mid-year introduction of the goods and services tax.

In Sub-Saharan Africa (SSA), growth accelerated by 2.7 per cent above the 1.4 per cent recorded in 2016, due to improved performance in the region's two largest economies, Nigeria and South Africa. The Nigerian economy expanded by 0.8 per cent from a contraction of 1.6 per cent in 2016 as the economy emerged from recession, owing to recovery in oil production and prices as well as ongoing strength in the agricultural sector. The South African economy expanded by 0.9 per cent from 0.3 per cent in 2016 driven by easing of drought in the agriculture sector and improved mining activity.

6.2 Outlook for Global Output

Global growth forecasts for 2018 was revised upwards due to expectations of improvements in macroeconomic conditions anchored on several factors including: favourable financial conditions and strong sentiments about investment demand. Other factors include the recovery of oil and other commodity prices expected to continue into the medium term; expectations of expansionary fiscal policy In the U.S and resolution of the NAFTA agreement by the U.S. with Canada and Mexico. These factors could be moderated by continued geo-political tensions in the Middle East, threats of military action on the Korean peninsula and difficulties in the BREXIT negotiations.

In the advanced economies, growth is expected to be spurred by government policies such as tax reforms and fiscal stimulus in the US and stronger domestic demand and higher external demand in Europe and Japan. Global output will also be influenced by the prospects of growth pickup in emerging market economies. Accordingly, global growth is forecast to stabilize at 3.9 per cent in 2018 and 2019, up from 3.7 per cent in 2017.

Growth in the advanced economies is projected to stabilize at 2.3 per cent apiece in 2017 and 2018 and decline to 2.2 per cent in 2019, influenced by uncertainty surrounding continued normalization of US monetary policy, although moderated by expected improvements in business activities due to the response of investment to the proposed US tax cuts. The Euro area is forecast to slowdown as growth is projected at 2.2 and 2.0 per cent in 2018 and 2019 down from 2.4 per cent in 2017. The lower projection for the region is due to the possible impact of increased political uncertainty surrounding the BREXIT discussions, operating through confidence and demand channels. Growth projections for other advanced economies such as Japan and the United Kingdom, in 2018 and 2019, were also revised downwards mostly on account of a less-than-expected performance during the latter part of 2017. In addition, headwinds from the on-going BREXIT negotiations continue to impose a drag on growth in the United Kingdom, while Japan's ageing population is slowing down aggregate demand.

In the emerging market and developing economies, growth is projected at 4.9 and 5.0 per cent in 2018 and 2019, respectively, up from 4.7 per cent in 2017. The development is expected to be driven by improvements in economic conditions such as stronger external demand and commodity prices. Growth forecast for India is projected at 7.4 and 7.8 per cent in 2018 and 2019, respectively, up from 6.7 per cent in 2017. The Brazilian economy is expected to experience stronger recovery of 1.9 and 2.1 per cent in 2018 and 2019, respectively, compared with 1.1 per cent in 2017, due to increasing commodity prices and easier financing conditions. Growth in China is, however, expected to decline slightly to 6.6 and 6.4 per cent in 2018 and 2019, respectively, from 6.8 per cent in 2017.

In sub-Saharan Africa, growth is forecast to rise to 3.3 and 3.5 per cent in 2018 and 2019, respectively, up from 2.7 per cent in 2017. The expected improvement would result from modest output expansion in Nigeria in the face of a subdued growth prospect in South Africa. Nigeria is projected to grow by 2.1 and 1.9 per cent in 2018 and 2019, respectively, up from 0.8 per cent in 2017; while growth in South Africa is projected to remain stable at 0.9 per cent during 2017 - 2019.

In the Middle East and North Africa (MENA) region, higher growth forecasts of 3.6 and 3.5 per cent in 2018 and 2019, respectively, are expected, up from 2.5 per cent in 2017. The stronger growth is likely to result from firmer crude oil prices and increase in domestic demand among the oil producing countries in the region, particularly Saudi Arabia.

6.3 Downside Risks to Global Outlook

In the medium term, risks to the global economic outlook would continue to be tilted to the downside. These downside risks include: the potential build-up of vulnerabilities, given the current easy financing conditions. These vulnerabilities could accumulate as yield-seeking investors increase exposures to riskier corporate and sovereign borrowers and less credit-worthy households. Another risk is the possible adoption of inward-looking trade policies. In particular, the likely increase in trade barriers and regulatory realignments, following on-going NAFTA renegotiations and BREXIT discussions, could dampen investment and undermine production and trade efficiencies globally in the medium term. In the advanced economies, risks to the outlook include ensuring the sustainability of public debt and curtailing excessive external imbalances.

In the emerging market and developing economies, rebuilding fiscal buffers, especially in commodity-dependent economies remains a key challenge to investment and growth in the medium term. With adequate fiscal buffers, exchange rate flexibility could complement other policy measures to prevent sustained misalignments of relative prices in the domestic economy, and the build-up in external imbalances.

The medium-term global outlook is also clouded by geopolitical tensions, notably in East Asia and the Middle East. In addition, non-economic factors could threaten near term growth prospects. In this regard, recent extreme weather outcomes, including hurricanes in the Atlantic and drought in Sub-Saharan Africa and Australia, signpost the risk of climatic events destabilizing economic activities with devastating humanitarian costs and economic losses to the affected regions. The development could add to migration flows that further destabilizes already fragile recipient economies.

In the Middle East and North Africa, continued civil unrest and hostilities which had undermined economic activities are unlikely to recede in the near term. These include: armed conflicts, emergence of militia groups, and growing population of displaced persons as well as increasing geopolitical tensions and terrorism, which are likely to undermine confidence and dampen growth and investment.

Table 6.1
Global Output and Inflation Outlook

	2015	2016	2017	2018*
A. World Output				
World Output	**3.2**	**3.2**	**3.7**	**3.9**
Advanced Economies	**2.1**	**1.7**	**2.3**	**2.3**
USA	2.6	1.5	2.3	2.7
Euro Area	2.0	1.7	1.6	1.6
Japan	1.2	0.9	0.8	0.5
UK	2.2	2.0	1.5	1.4
Canada	0.9	1.3	1.9	2.0
anced Economies	2.0	1.8	2.4	2.2
Emerging & Developing Economies	**4.1**	**4.4**	**4.7**	**4.9**
Commonwealth of Independent States	-2.8	0.4	2.2	2.2
Latin America and the Caribbean	0.1	-0.7	1.3	1.9
Middle East and North Africa	2.5	4.9	2.5	3.6
Sub-Saharan Africa	3.4	1.4	2.7	3.3
B. Commodity Prices (US' Dollars)				
Oil	-47.2	-15.7	23.1	11.7
Non-fuel	-17.4	-1.6	6.5	-0.5
C. Consumer Prices				
Advanced Economies	0.3	0.8	1.7	1.9
Emerging & Developing Economies	4.7	4.3	4.1	4.5

Source: IMF WEO Update, January 2018
*Forecast

6.4 Global Inflation Outlook

Globally, consumer prices are projected to rise modestly from 3.1 per cent to 3.3 per cent in 2018, partly reflecting rising oil and other commodity prices. The increase is, however, likely to remain subdued due to persisting output gaps in many advanced and emerging market economies.

In the advanced economies, inflation is forecast to remain stable at 1.7 per cent in 2017 and 2018, due to remarkably lower wage growth and slack in the labour market. Inflation in the United States remained unchanged at 2.1 per cent in 2017 and 2018, driven by rise in energy prices, moderated by recent appreciation of the domestic currency. In the United Kingdom, inflation is projected to remain stable at 2.6 per cent in 2017 and 2018, fuelled by mixed factors including BREXIT uncertainty. In the Euro Area, although inflation remained below its 2.0 per cent target, it is forecast to fall to 1.4 per cent in 2018, from 1.5 per cent in 2017, largely on account of the decline in German inflation from 1.6 to 1.5 per cent over the same period.

In the emerging market and developing economies, inflation is expected to rise to 4.4 per cent in 2018, from 4.2 per cent in 2017. In China, it is projected to rise to 2.4 per cent in 2018, from 1.8 per cent in 2017, reflecting the effects of modest recovery in oil and other commodity prices. In India, it is expected to rise to 4.9 per cent in 2018, from 3.8 per cent in 2017. In Brazil, inflation is projected to increase to 4.0 per cent in 2018, from 3.7 per cent in 2017. The decline in food prices and high excess capacity in the economy would moderate the rise in price levels in both Brazil and India. In Russia, inflation is forecast to decline to 3.9 per cent in 2018 from 4.2 per cent in 2017, due to rising oil prices feeding into currency appreciation.

Inflation in Sub-Saharan Africa is forecast to decline to 9.5 per cent in 2018, from 11.0 per cent in 2017, owing to moderation in currency depreciations from a combination of factors including firming up of oil and other commodity prices. Inflation in Nigeria is projected to decline to low sing digit between 11 - 14.8 per cent in 2018, from 16.3 per cent in 2017, driven by rising oil receipts passing through to lower domestic prices. In South Africa, inflation is projected to decline to 5.3 per cent in 2018 from 5.4 per cent in 2017, driven by expected decline in food, and housing & utilities prices.
Inflation in the Middle East, North Africa is forecast to rise to 8.1 per cent in 2018 from 7.1 in 2017, driven by depreciations of domestic currencies, the removal of subsidies, and increase in value-added taxes.

6.5 Outlook for Domestic Output Growth

Output growth in the second half of 2017 was positive, following the exit from recession in the second quarter of 2017. Real GDP in the fourth quarter of 2017 strengthened further by 1.92 per cent from the growth of 1.40 per cent in the preceding quarter of 2017, in contrast to the contraction of 1.73 per cent in the corresponding quarter of 2016 on the back of higher crude oil production and growth of the non-oil sector.

The increase in GDP growth has been attributed to several factors, including the moderate rise in crude oil prices and improvement in oil production following the relative peace in the Niger Delta region.

The economy is projected to remain on a growth path into the first half of 2018, supported by positive developments in the oil sector and other government initiatives conducive to growth. The oil sector is poised to benefit from improved and stable production from OPEC's commitment to its output cut agreement. Also the prevailing peace deal between the Federal Government of Nigeria and stakeholders in the Niger Delta is expected to continue to support oil production. The recovery in oil price and improved Joint Venture production will help support government revenue, with the latter adding approximately 0.2 million barrels per day to total oil production in 2018. Furthermore, the non-oil sector would benefit from fiscal spending following the implementation of the 2018 budget, as well as various development finance initiatives of the Bank. The CBN's commitment to make foreign exchange available to genuine businesses and retail users is expected to support manufacturing sector output and spur overall expansion of goods and services production in the economy.

Based on the foregoing, the growth outlook for the economy is largely optimistic. The International Monetary Fund (IMF) forecasts Nigeria's output growth in 2018 at 2.1 per cent from 0.8 per cent in 2017 (IMF, WEO, January 2018), premised on expected stronger activity and the positive effect of restriction on OPEC oil production. Similarly, the World Bank forecasts Nigeria's growth at 2.5 per cent in 2018 up from 1.0 per cent in 2017, premised on the sustenance of rising oil production and continuing reforms in the foreign exchange market, coupled with improved electricity supply. Also, the Federal Government of Nigeria's 2018 appropriation bill is based on the growth forecast of 3.5 per cent.

The key risks to the promising growth outlook, however, remain developments in the external environment which may affect capital inflow to Nigeria, as well as domestic economic conditions. The key domestic risks include the delay in the passage and implementation of the FGN 2018 budget, thereby denying the economy of needed fiscal stimulus. In addition, slow credit growth and poor transmission the monetary policy impulses to the real economy is clearly undermining output. The perennial challenge of infrastructural deficit remains a constraint to entrepreneurial activities and initiatives in the economy. Also, external sector imbalances could widen and harm growth if the current oil price outlook and stability in the Niger Delta region reverses in the near term. It is, however, hoped that monetary, fiscal and trade policies would focus on these challenges in order to support the fragile recovery in the near term.

6.6 Outlook for Domestic Inflation

Nigeria's headline inflation (year-on-year) moderated during the second half of 2017, although still substantially above the Bank's benchmark of 6-9 per cent. The price development, however, remained within the lower double-digit range and is unlikely to harm growth, based on available inflation threshold studies for the economy. Staff estimates indicate that year-on-year headline inflation is expected to continue decelerating to 15.35, 14.45 and 13.25 per cent in January, March and June 2018, respectively, driven by sustained stability in the foreign exchange market, lower food prices and the sustained tight monetary policy stance of the Bank.

The upside risk to inflation would include: the implementation of the proposed expansionary 2018 Federal Government budget and election-related spending in preparation for the 2019 general elections in the country. Also, continued poor power supply, increased cost of transportation, the disruptive effects of the clashes between farmers and herdsmen, amongst others, are likely to feed into higher domestic prices, thereby moderating the current deceleration in inflation. The Bank would, however, continue to manage liquidity conditions in the domestic economy to ensure that these threats from inflation are minimized.

Summary of Inflation Forecast for Year-On-Year Change (per cent)

	YEAR-ON-YEAR INFLATION RATE					12-MMA INFLATION RATE			
Status	Month	Headline inflation	Food inflation	Core inflation	Status	Month	Headline inflation	Food inflation	Core inflation
Actual	Jul-17	16.05	20.28	12.21	Actual	Jul-17	17.48	18.25	15.80
	Aug-17	16.01	20.25	12.30		Aug-17	17.33	18.57	15.34
	Sep-17	15.98	20.32	12.12		Sep-17	17.17	18.88	14.90
	Oct-17	15.91	20.31	12.14		Oct-17	16.97	19.14	14.41
	Nov-17	15.90	20.31	12.21		Nov-17	16.76	19.39	13.93
	Dec-17	15.37	19.42	12.09		Dec-17	16.50	19.55	13.46
Forecast	Jan-18	15.35	19.40	12.15	Forecast	Jan-18	16.24	19.66	13.01
	Feb-18	15.01	18.95	12.07		Feb-18	16.01	19.68	12.71
	Mar-18	14.45	18.28	11.04		Mar-18	15.78	19.65	12.35
	Apr-18	14.23	18.34	10.53		Apr-18	15.53	19.56	12.01
	May-18	13.42	17.22	10.20		May-18	15.28	19.37	11.77
	Jun-18	13.25	17.71	9.34		Jun-18	15.04	19.18	11.50

Source: CBN Statistics Dept.

6.7 Outlook for Monetary Policy in 2018

The medium term outlook for the economy indicated a modest recovery from the current fragile growth. The outlook will be substantially driven by the sustained implementation of the Federal Government's Economic Recovery and Growth Plan (ERGP) within an overall context of expansionary fiscal policy. The non-oil sector is expected to play a major role in the recovery prospect, supported by the sustained development finance initiatives and financial inclusion strategies of the Bank, in addition to other initiatives by government to diversify the economy. Also, the prospects for continuing moderation in inflation outcomes would be strengthened by the commitment of the monetary authority to continue to implement appropriate liquidity management measures and supportive foreign exchange policies. In this regard, the policy challenge facing the economy is sustaining the fragile growth in the face of still high, although moderating inflationary pressures.

Accordingly, the risks to monetary policy in the near-term would include: the high but moderating inflationary pressure, as well as banking system liquidity surfeit and weakening macro-prudential indicators that are likely to threaten financial system stability. Others include: sustaining the fragile stability in the foreign exchange market in the face of continued normalization of monetary policy by some advanced economies; contraction in private sector credit in the face of sluggish recovery; high unemployment rate; and rising costs and shortages of energy. On the fiscal front, the rising debt profile of the Federal and sub-national governments and uncertainty surrounding the passage and implementation of the expansionary 2018 Federal Government budget as well as election-related spending in the run-up to the 2019 general elections, are clearly key concerns. The Bank would continue to design, implement and monitor appropriate monetary policy measures to ensure that the downside risks stemming from inflation to growth are reined-in in the near to medium term.

Appendices

CENTRAL BANK OF NIGERIA COMMUNIQUÉ NO 114 OF THE MONETARY POLICY COMMITTEE MEETING OF 24th AND 25th JULY, 2017

1.0 Background

The Monetary Policy Committee met on the 24th and 25th of July 2017, against the backdrop of a relatively improving global economy. However, protectionism in trade and immigration; fragilities in the financial markets, remain the key risks to global economic stability.

On the domestic front, the economy is on a path to moderate recovery with a positive short- to medium-term outlook, premised largely on fiscal stimulus and a stable naira exchange rate. Inflation expectations also appear sufficiently anchored with the current stance of monetary policy.

In attendance were 8 out of 12 members of the Committee. The Committee examined the global and domestic economic and financial environments in the first half of 2017 and the outlook for the rest of the year.

External Developments

The momentum witnessed in the global economy in Q1 2017 continued through the second quarter, driven by a generally accommodative monetary policy stance in most advanced economies, moderation in energy prices and improved global demand. The emerging markets and developing economies, are experiencing positive spillovers from somewhat improved commodity prices and developments in the advanced economies. The growth prospects for this group of countries in 2017 are expected to rise to about 4.6 per cent from 4.3 per cent in 2016.

Complemented by the momentum in other blocks and a potential positive prospect for expansion in world trade, the IMF in its July edition of the World Economic Outlook (WEO) projected global output growth in 2017 at 3.5 per cent from 3.1 per cent in 2016.

The MPC, however, noted some headwinds confronting the optimistic outlook to global growth arising mainly from receding market expectations of expansionary U.S. fiscal policy, weaker than expected growth in the U.K due to difficult BREXIT negotiations and geo-political risks associated with the forthcoming German general elections. In addition, the Committee noted the downward trend in global inflation after earlier indications of an uptick as the U.S. continues to build up inventories in shale oil, while emerging economies such as Brazil, Russia and South Africa witness strong economic headwinds leading to sharp downturn in output.

Domestic Output Developments

Data from the National Bureau of Statistics (NBS) showed that the contraction in the economy moderated to 0.52 per cent in Q1 2017 from 1.30 per cent in Q4 2016. The data further revealed that fifteen economic activities recorded positive growth in Q1 2017, showing strong signs of recovery. The Purchasing Managers Index (PMI) for manufacturing and non-manufacturing activities stood at 52.9 and 54.2 index points in May and June 2017, respectively from 52.7 and 52.5 index points in May 2017, indicating an expansion for the third consecutive month. Similarly, the Composite Index of Economic Activities (CIEA) rose from 55.85 to 59.50 index points between April and June 2017. The Committee noted the continuous positive effects of improved foreign exchange management on the performance of manufacturing and other economic activities. Non-oil real GDP grew by 0.72 per cent in Q1 2017, reflecting growth in the agricultural sector by 0.77 per cent in the same period. Provisional data also showed that the external sector remained resilient in Q2 2017, as the overall Balance of Payments (BOP) position recorded a surplus of US$0.65 billion, equivalent to 0.8 per cent of GDP. The Committee hopes that the implementation of the 2017 budget and the Economic Recovery & Growth Plan (ERGP) will further strengthen growth and stimulate employment.

Developments in Money and Prices

The Committee noted that money supply (M2) contracted by 7.33 per cent in June 2017, annualized to a contraction of 14.66 per cent, in contrast to the provisional growth benchmark of 10.29 per cent expansion for 2017. The development in M2 reflected a contraction of 7.45 per cent in net foreign assets (NFA) in June 2017. Similarly, M1 contracted by 7.98 and 10.70 per cent in May and June 2017, respectively, consistent with the directive of the MPC that expansion in narrow money should be controlled. On the other hand, net domestic credit (NDC) grew modestly by 1.02 per cent in June 2017, (annualized at 2.04 per cent), driven mainly by net credit to government, which grew by 5.91 per cent. Credit to the private sector, however, declined relative to end-December 2016 by 0.02 per cent. The MPC noted the widening fiscal deficit of N2.51 trillion in the first half of 2017 and the growing level of government indebtedness and expressed concern about the likely crowding out effect on private sector investment. The constrained growth in the monetary aggregates provides evidence of weak financial intermediation in the banking system arising from the constraints imposed by developments in the macroeconomy.

Headline inflation (year-on-year) declined for the fifth consecutive month in June 2017, to 16.10 per cent from 16.25 per cent in May, and 18.72 per cent in January 2017. Core inflation moderated to 12.50 per cent in June from 13.00 per cent in May 2017 while the food index rose marginally to 19.91 per cent in June from 19.27 per cent in May 2017. This development was traced to intermittent attacks by herdsmen on farming communities, sporadic terrorist attacks in the North-East and other seasonal farming effects. The Committee was particularly concerned about the unabating pressure from food inflation but hopeful that the situation will dampen in the third quarter as harvests begin to manifest.

The Committee also attributed the moderation in inflation to be partly due to the effects of the relative stability in the foreign exchange market, stemming from improved management, which promoted increased inflows. Against this backdrop, the Committee reiterated its commitment to sustain and deepen flexibility in the foreign exchange market to further enhance foreign exchange flow in the economy. The Committee, however, noted the protracted effects of high energy and transportation costs as well as other infrastructural constraints on consumer price developments and expressed hope that government will fast-track its reform agenda to address these legacy issues. The Committee noted that while responding to the current tight monetary policy stance, inflation still had a strong base effect which is expected to wane by August 2017.

Money market interest rates moved in tandem with the high level of liquidity in the banking system. The interbank call rate opened at 16.13 per cent on May 25, 2017 and closed at 4.43 per cent on June 29, 2017. However, the average inter-bank call rate during the period stood at 12.49 per cent. The movement in the net liquidity position reflected the effects of OMO, foreign exchange interventions, statutory allocation to state and local governments, and maturity of CBN Bills.

The Committee noted the improvements in the equities segment of the capital market as the All-Share Index (ASI) rose by 33.33 per cent from 25,516.34 on March 31, 2017, to 34,020.37 on July 21, 2017. Similarly, Market Capitalization (MC) rose by 32.84 per cent from N8.83 trillion to N11.73 trillion during the same period. Relative to end-December 2016, capital market indices rose by 26.59 and 26.81 per cent, respectively, reflecting growing investor confidence due to improvements in foreign exchange management. The Committee however, noted the seeming bubble in the capital market and cautioned on the utilization of the inflows.

Total foreign exchange inflows through the Central Bank of Nigeria (CBN) increased by 35.41 per cent in June 2017 compared with the previous month. Total outflows, on the other hand, decreased by 12.73 per cent during the same period, as a result of reduced CBN intervention in the interbank foreign exchange market, which also reduced TSA (dollar) payments balances by 61.4 per cent in the period under review. The positive net flows resulted in an improvement of gross external reserves to $30.30 billion at end-June 2017, compared with $29.81 billion at end-May 2017.

The Committee noted the emerging convergence between the bureau-de-change (BDC) and Nigeria Autonomous Foreign Exchange (NAFEX) segment rates and the stability of the average naira exchange rate at the inter-bank segment of the foreign exchange market during the review period.

2.0. Overall Outlook and Risks

Available forecasts of key macroeconomic indicators point to a fragile economic recovery in the second quarter of the year. The Committee cautioned that this recovery could relapse in a more protracted recession if strong and bold monetary and fiscal policies are not activated immediately to sustain it. Thus, the expected fiscal stimulus and non-oil federal receipts, as well as improvements in economy-wide non-oil exports, especially agriculture, manufacturing, services and light industries, all expected to drive the growth impetus for the rest of the year must be pursued relentlessly. The Committee expects that timely implementation of the 2017 Budget, improved management of foreign exchange, as well as security gains across the country, especially, in the Niger Delta and North Eastern axis, should be firmly anchored, to enhance confidence and sustainability of economic recovery.

The Committee identified the downside risks to this outlook to include weak financial intermediation, poorly targeted fiscal stimulus and absence of structural programme implementation.

3.0. The Considerations of the Committee

Notwithstanding the improved outlook for growth, the Committee assessed the implications of the uncertainties arising from the continued normalization of monetary policy by the US Fed and the implications of a strong dollar, the weak recovery of commodity prices, and the uncertainty of US fiscal policy. The Committee similarly evaluated other challenges confronting the domestic economy and the opportunities for achieving economic growth and price stability in 2017.

The Committee expressed satisfaction with the gradual but consistent decline in inflationary pressures in the domestic economy, noting its substantial base effect, continuous improvements in the naira exchange rate across all segments of the foreign exchange market, and considerable signs of improved investments inflows. The Committee welcomed the move by the fiscal authorities to engage the services of asset-tracing experts to investigate the tax payment status of 150 firms and individuals in an effort to close some of the loopholes in tax collection, towards improving government revenue. However, the Committee expressed concern about the slow implementation of the 2017 Budget and called on the relevant authorities to ensure timely implementation, especially, of the capital portion in order to realize the objectives of the Economic Recovery and Growth Plan.

The MPC believes that at this point, developments in the macroeconomy suggest two policy options for the Committee: to hold or to ease the stance of monetary policy.

Against the backdrop of the outlook for the domestic and global economy; the enthusiasm around the base-effect which reduced inflationary pressures and the continuous relative stability in the naira exchange rate, there is need to maintain cautious optimism, given the potential ramification of a major deviation from the existing policy path. The Committee is not unmindful of the high cost of capital and its implications on the still ailing economy, which arguably necessitates an accommodating monetary policy stance. The MPC also noted the liquidity surfeit in the banking system and the continuous weakness in financial intermediation, but agreed on the need to support growth without jeopardizing price stability or upsetting other recovering macroeconomic indicators, particularly the relative stability in the foreign exchange market.

The MPC thinks that easing at this point would signal the Committee's sensitivity to growth and employment concerns by encouraging the flow of credit to the real economy. It would also promote policy consistency and credibility of its decisions. Also, the Committee observed that easing at this time would reduce the cost of debt service, which is actually crowding out government expenditure. The risks to easing however, would show in terms of upstaging the modest stability achieved in the foreign exchange market, the possible exit of foreign portfolio investors as well as a resurgence of inflation following the intensified implementation of the 2017 budget in the course of the year. The Committee also reasoned that easing would further pull the real interest rate down into negative territory.

The argument for holding is largely premised on the need to safeguard the stability achieved in the foreign exchange market, and to allow time for past policies to work through the economy. Specifically, the MPC considered the high banking system liquidity level; the need to continue to attract foreign investment inflow to support the foreign exchange market and economic activity; the expansive outlook for fiscal policy in the rest of the year; the prospective election related spending which could cause a jump in system liquidity, etc.

The MPC expressed concern over the increasing fiscal deficit estimated at N2.51 trillion in the first half of 2017 and the crowding out effect of high government borrowing. While urging fiscal restraint to check the growing deficit, the Committee welcomed the proposal by government to issue sovereign-backed promissory notes of about N3.4 trillion for the settlement of accumulated local debt and contractors arrears. The Committee, however, advised the Management of the Bank to monitor the release process of the promissory notes to avoid an excessive injection of liquidity into the system thereby offsetting the gains so far achieved in inflation and exchange rate stability.

On the outlook for financial system stability, the Committee noted that, in spite of the resilience of the banking sector, the prolonged weak macroeconomic environment has continued to impact negatively on the sector's stability. The MPC reiterated its call on the Bank to sustain its intensive surveillance of deposit money banks' activities for the purpose of promptly identifying and addressing vulnerabilities. The Committee also called on the DMBs to support economic recovery and growth by extending reasonably priced credit to the private sector.

4.0. The Committee's Decisions

In consideration of the headwinds confronting the domestic economy and the uncertainties in the global environment, the Committee decided by a vote of 6 to 2 to retain the Monetary Policy Rate (MPR) at 14.0 per cent alongside all other policy parameters. Consequently, 6 members voted to retain the MPR and all other parameters at their current levels while two members voted to ease the stance of monetary policy. In summary, the MPC decided to:

(i) Retain the MPR at 14 per cent;
(ii) Retain the CRR at 22.5 per cent;
(iii) Retain the Liquidity Ratio at 30.00 per cent; and
(iv) Retain the Asymmetric corridor at +200 and -500 basis points around the MPR.

Thank you for listening.

Godwin I. Emefiele
Governor, Central Bank of Nigeria
25th July, 2017

CENTRAL BANK OF NIGERIA COMMUNIQUÉ NO 115 OF THE MONETARY POLICY COMMITTEE MEETING OF 25th AND 26th SEPTEMBER, 2017

1.0 Background

The Monetary Policy Committee met on the 25th and 26th of September, 2017 against the backdrop of a relatively optimistic global economy. The Committee examined the global and domestic economic and financial environments up to the third quarter of 2017, and the outlook for the rest of the year. The recent spate of flooding and hurricanes in some parts of the globe; the flooding in Nigeria; the increasing tension between the US and North Korea, and the perception of hostilities on the Korean Peninsula as well as the associated geo-political tensions, were identified as key risks to global output growth.

On the domestic front, the economy exited recession (which began in the first quarter of 2016) in the second half of 2017, with a modest positive short to medium-term outlook, resulting largely from deliberate macroeconomic stimulus and a stable naira exchange rate. Inflation expectations also appeared anchored on the strength of prevailing tight monetary policy stance.

Seven (7) members of the MPC were present at the meeting.

External Developments

Global output is projected to improve further in 2017, as growth forecast by the IMF in its July World Economic Outlook (WEO) was projected at 3.5 per cent, up from 3.2 per cent in 2016. Output growth in some advanced economies, including Japan, the Euro-area as well as some emerging market and developing economies is expected to improve in 2017. Nigeria, Brazil and South Africa, all exited recession, while Russia is likely to exit recession in the fourth quarter of 2017, after a mild contraction of 0.57 per cent in the second quarter. Growth forecast for the US was revised downwards from 2.3 per cent to 2.1 per cent in 2017, as a result of the weak growth observed in the first quarter of the year.

The MPC, however, noted some headwinds confronting the optimistic global growth prospects to include: recent developments on the Korean peninsula; the damage to infrastructure caused by hurricanes - Harvey, Irma and Maria; the lull in BREXIT negotiations and the normalization of monetary policy by the US Fed, which is expected to instigate global capital flow reversal. Other challenges include the continued slow pace of recovery in global oil and other commodity prices and China's reduction in uptake of global commodities. In addition, the Committee noted the tepid global inflation momentum, implying that continued monetary policy normalization could be injurious to global growth prospects.

The uptick in global inflation persisted, but moderated, in response to rising oil prices, continued accommodative monetary policy in the advanced economies; and currency appreciation in some emerging markets and developing countries. Average inflation for the developed economies is projected at 1.9 per cent in 2017, while it is forecast to average 4.5 per cent in the emerging and developing economies, as prices are expected to moderate due to seasonal effects. The Committee observed that the outlook for global monetary policy remains predominantly accommodative, in support of recovery and growth.

Domestic Output Developments

Data from the National Bureau of Statistics (NBS) showed that real Gross Domestic Product (GDP) grew by 0.55 per cent in the second quarter of 2017, against the contractions of 0.91 and 1.49 per cent in the previous quarter of 2017, and the corresponding quarter of 2016, respectively, marking the technical exit of the Nigerian economy from recession. Non-oil real GDP grew by 0.45 per cent in Q2, 2017, driven largely by agriculture (3.0%), industry (1.1%), and construction (0.1%). The modest growth was attributed to fiscal injections from the implementation of the Economic Recovery and Growth Plan (ERGP), and enhanced supply of foreign exchange arising from improved crude oil prices. The Committee also noted the positive outlook from the Purchasing Managers Index (PMI) for manufacturing and non-manufacturing activities, which stood at 53.6 and 54.1 index points in August 2017, respectively, above the 50 index points benchmark, indicating moderate signs of recovery. The Committee further noted that, although the recovery was weak, it was hopeful that the active implementation of the 2017 budget could boost aggregate demand and employment.

Developments in Money and Prices

The Committee noted that money supply (M2) contracted by 11.06 per cent in August 2017 (annualised), in contrast to the provisional growth benchmark of 10.29 per cent for 2017. The development in M2 is largely due to the contraction of 18.42 per cent in other assets net (OAN) in August 2017. Similarly, M1 contracted by 12.25 per cent in August 2017, (annualised to -18.37 per cent). Net domestic credit (NDC) contracted by 0.14 per cent, annualized at -0.20 per cent, driven majorly by net credit to government, which also contracted by 1.05 per cent against the programmed growth of 33.12 per cent. Credit to the private sector, however, grew marginally by 0.07 per cent in August 2017, compared with the provisional benchmark of 14.88 per cent. The MPC also noted the policy constraints in ensuring the flow of credit to the real sector in the face of weak and underperforming monetary aggregates.

Inflationary pressure in the economy continued to moderate with headline inflation (year-on-year) receding for the seventh consecutive month to 16.01 per cent in August 2017, from 16.05 per cent in July 2017. Food inflation declined slightly to 20.25 per cent in August 2017 from 20.28 per cent in July 2017, while core inflation increased to 12.30 per cent in August 2017 from 12.21 per cent in July 2017. This development was attributed to the contraction in money supply, decline in imported food and non-food prices, favourable base effects, and the moderating effects of stable exchange rates. The Committee, however, noted that the high food inflation was traceable to rising prices of farm inputs and supply shortages, intermittent clashes between farmers and herdsmen, as well as weak harvest, due to increased flooding of farmlands.

Money market interest rates oscillated in tandem with the level of liquidity in the banking system as the average inter-bank call rate which opened at 18.00 per cent on July 26, 2017, closed at 7.00 per cent on August 31, 2017. The OBB rate opened at 15.03 per cent and closed lower at 7.83 per cent in the same period. However, the average inter-bank call and OBB rates for the period stood at 22.63 and 39.66 per cent, respectively. The movement in net liquidity positions and flows reflected the effects of OMO sales; foreign exchange interventions; statutory revenue payments to states and local governments; remittances by Nigerian Customs and Federal Inland Revenue Services for FAAC meetings; and the maturity of CBN Bills.

The Committee noted the continuing improvement in the external reserves position and the equities segment of the capital market. External reserves position grew to US$32.9 billion at close of business on 25th September, 2017 while the All-Share Index (ASI) rose by 7.20 per cent from 33,117.48 on June 30, 2017 to 35,504.62 on August 31, 2017. Market Capitalization (MC) improved by 6.90 per cent to N12.24 trillion from N11.45 trillion during the same period. Relative to end-December 2016, capital market indices rose by 32.10 and 32.30 per cent, respectively, reflecting growing investor confidence, due to improvements in foreign exchange management.

Total foreign exchange inflows through the Central Bank of Nigeria (CBN) rose by 1.98 per cent in August 2017, compared with the previous month. Similarly, total outflow increased by 7.03 per cent during the same period, as a result of increased international remittances, inclusive of public sector and JVC payments; which rose by 58.59 per cent in the period under review.

The Committee noted the trend towards convergence between the rates at the bureau-de-change (BDC) and the Nigeria Autonomous Foreign Exchange (NAFEX) segments, as well as the stability of the exchange rate at the inter-bank segment of the foreign exchange market during the review period. Similarly, the Committee noted the success of the Investor and Exporters' window (I &E) of the foreign exchange market and traced this not only to foreign investor confidence but also to the zeal and commitment of Nigerian exporters who have demonstrated preference for the window to the parallel market. The Committee observed that the I&E window has increased liquidity and boosted confidence in the market with over US$7.0 billion inflow in the last five months. The Committee will continue to introduce policies that will improve the confidence of foreign investors in the country's macroeconomic management regime.

2.0. Overall Outlook and Risks

Available data and forecast of key macroeconomic variables indicate a relatively positive outlook, predicated on existing policy initiatives including the ERGP. Other potential drivers of economic recovery are; the expected increase in government revenue arising from favourable crude oil prices, stable output, and general improvements in the non-oil sector, especially, agriculture, industry and construction. The intervention by the CBN in the real sector is expected to continue to yield positive results in terms of output and lower consumer prices.

The Committee, however, noted some downside risks to the overall short- to medium-term positive outlook for the economy. These include; flooding which displaced farming communities and political agitations. On the external front, the hawkish policy stance in the United States, rising geo-political tensions and sluggish output recovery in the Euro-area and Japan, could slow-down the momentum of global output growth, with significant spillovers to emerging markets and developing countries, including Nigeria.

3.0. The Considerations of the Committee

The Committee applauded the exit of the Nigerian economy from recession but observed that the growth remains fragile and, therefore, hopes that complementary fiscal and monetary policies would sustain the growth momentum. The Committee further expressed satisfaction with the gradual, but consistent decline in inflation, noting, however, the substantial base effect in addition to the continuous improvement in the naira exchange rate across all segments of the foreign exchange market; and considerable improvement in foreign capital inflow. The Committee welcomed the steady implementation of the 2017 Budget, especially, the capital component of the budget, and urged increased momentum in expenditure directed at the growth-stimulating sectors of the economy in order to reduce youth unemployment and restiveness.

The Committee, however, expressed concern on the sustained pressure on food prices, noting risks posed by floods, strikes and insurgencies in various parts of the country to food production and distribution. Regarding the tepid turnaround in economic activities in the second quarter of 2017, the Committee emphasized that the employment gains of recovery were still minimal, noting that a number of important job elastic sub-sectors were still weak and may require more fiscal support to regain traction. The Committee, however, commended the Federal Government for issuing the Executive Order aimed at improving the ease of doing business in the country. It also noted the efforts of the government to create jobs in the agricultural sector with the inauguration of the Presidential Committee on job creation, targeting at least ten thousand jobs in each state of the Federation, over the next six months through a boost in agricultural support and funding. The Committee enjoins the state governments to work with the Presidential Committee to actualise this plan without further delay.

The MPC also noted with satisfaction, the directive of the Federal Government to all states to promptly pay outstanding salary arrears, in order to boost aggregate demand. It commended efforts to clear outstanding contractor arrears; prompt settlement of trade disputes with certain Unions of organised labour, including the Academic Staff Union of Universities (ASUU) and Health Workers; as well as the release of money to settle outstanding entitlements of the erstwhile workers of the defunct Nigeria Airways. These efforts, the Committee reasoned would improve aggregate demand and strengthen the weak recovery.

The Committee restated its commitment to maintaining stability in prices, without which meaningful recovery cannot be achieved. In this regard, members welcomed the gradual narrowing of rate spreads in the foreign exchange market and urged the Bank to continue to monitor and respond proactively to threats and vulnerabilities in the foreign exchange market.

On the outlook for financial stability, the Committee noted that, in spite of the banking sub-sector's resilience, the weak macroeconomic environment has continued to impact negatively on the stability of the sub-sector. The Committee reiterated its call on the Bank to sustain its surveillance of deposit money banks (DMBs) activities for the purpose of prompt identification and mitigation of potential vulnerabilities. The Committee also called on the DMBs to support the quest to move the economy forward by extending reasonably low priced credit to the private sector.

4.0. The Committee's Decisions

In arriving at its decision, the Committee took note of the gains so far achieved as a result of its earlier decisions; including the stability in the foreign exchange market and the moderate reduction in inflation. The option was whether to hold, tighten or ease. These were subjected to extensive debate. As in previous meetings, although tightening would help rein in inflation expectations and strengthen the stability in the foreign exchange market, the Committee felt that it would further widen the income gap, depress aggregate demand and adversely affect credit delivery to the private sector. The Committee also noted that tightening may result in the deposit money banks re-pricing their assets and loans, thus raising the cost of borrowing and therefore heightening the already weak investment climate and non-performing loans.

With respect to loosening, the Committee believed that while it would make it more attractive for Nigerians to acquire assets at cheaper prices, thus increasing their net wealth, and therefore stimulate spending as confidence rises, it nevertheless, felt constrained that loosening at this time would exacerbate inflationary pressures and worsen the exchange rate and inflationary conditions. The Committee also felt that loosening will further pull the real rate deeper into negative territory as the gap between the nominal interest rate and inflation widens.

On the argument to hold, the Committee believes that the effects of fiscal policy actions towards stimulating the economy have begun to manifest as evident in the exit of the economy from the fifteen-month recession. Although still fragile, the fragility of the growth makes it imperative to allow more time to make appropriate complementary policy decisions to strengthen the recovery. Secondly, the Committee was of the view that economic activity would become clearer between now and the first quarter of 2018, when growth is expected to have sufficiently strengthened and gains in receding inflation, very obvious. The most compelling argument for a hold was to achieve more clarity in the evolution of key macroeconomic indicators including budget implementation, economic recovery, exchange rate, inflation and employment generation.

In consideration of the headwinds confronting the domestic economy and the uncertainties in the global environment, the Committee decided by a vote of 6 to 1 to retain the Monetary Policy Rate (MPR) at 14.0 per cent alongside all other policy parameters. In arriving at this HOLD decision, the MPC commits to employing maximum flexibility to guide the economy on the path to optimal growth. Consequently, 6 members voted to retain the MPR and all other parameters at their current levels, while one member voted to lower the MPR to signal an ease to the current stance of tight monetary policy. However, overall, majority of the members expressed a strong commitment to policy flexibility that would allow the Committee to promptly take the necessary actions that would promote overall macroeconomic stability and engender sustainable growth.

In summary, the MPC voted to:

(i) Retain the MPR at 14.0 per cent;
(ii) Retain the CRR at 22.5 per cent;
(iii) Retain the Liquidity Ratio at 30.0 per cent; and
(iv) Retain the Asymmetric corridor at +200 and -500 basis points around the MPR.

Thank you for listening.

Godwin I. Emefiele
Governor, Central Bank of Nigeria
26th September, 2017

CENTRAL BANK OF NIGERIA COMMUNIQUÉ NO 116 OF THE MONETARY POLICY COMMITTEE MEETING OF MONDAY 20th AND TUESDAY 21st NOVEMBER, 2017

1.0 Background

The Monetary Policy Committee met on the 20th and 21st of November, 2017 against the backdrop of a relatively optimistic global economic outlook. The Committee reviewed key developments in the global and domestic economies during the first ten months of 2017 and assessed the risks to price and financial stability in the short- to-medium term as well as outlook for the first half of 2018.

Nine (9) members of the MPC were present at the meeting.

External Developments

Global output is projected to improve to 3.6 per cent in 2017 from 3.2 per cent in 2016. The revised growth forecast reflects the uptick in global economic activity, strengthened by the recovery in oil and other commodity prices and leading to improved aggregate demand. Growth in the advanced economies is projected to improve to 2.2 per cent in 2017 from 1.7 per cent in 2016. Similarly, emerging markets and developing economies are forecast to grow at 4.6 per cent in 2017 up from 4.3 per cent in 2016. The MPC, however, noted some risks to the outlook for global growth to include: continued tension in the Korean Peninsula, complexities arising from the BREXIT negotiations and financial market uncertainties due to monetary policy normalization in the US.

The Committee noted that the pace of increase in inflation in the advanced economies, with the exception of the UK, is expected to be considerably slow towards the end of 2017. In the emerging market economies, inflationary pressures have abated as key economies exit recession and their currencies stabilize. Inflation is projected at 1.7 and 4.2 per cent in 2017 in the advanced and developing economies, respectively. The Committee observed that the outlook for global monetary policy remains largely accommodative, in support of economic recovery and growth.

Domestic Output Developments

Data from the National Bureau of Statistics (NBS) indicate that real Gross Domestic Product (GDP) grew by 1.40 per cent in the third quarter of 2017, up from 0.72 per cent, and contraction of 0.91 per cent in the second and first quarter of 2017, respectively. The major drivers of real GDP growth were agriculture (0.88%) and industry (1.83%). Some subsectors contracted, including: construction (0.01%), trade (0.29%) and services (1.02%). Overall, non-oil real GDP contracted by 0.76 per cent in Q3 2017, giving credence to the argument that more work is required to consolidate the recovery process; by putting in place policies that will boost growth through the non-oil sector.

The Committee also noted the continuous positive outlook based on the Manufacturing Purchasing Managers Index (PMI), which stood at 55.0 index points in October 2017, indicating expansion in the manufacturing sector for the seventh consecutive month. Eleven of the sixteen sub-sectors reported growth in the review period. Also, the composite PMI for the non-manufacturing sector stood at 55.3 index points in October 2017, indicating growth for the sixth consecutive month. The Committee hopes that, while the economic recovery appears to remain fragile, a tenacious implementation of the 2017 budget and quick passage of the 2018 budget would boost aggregate demand and confidence in the economy.

Developments in Money and Prices

The Committee noted that money supply (M2) contracted by 5.54 per cent in October 2017 (annualized), in contrast to the provisional growth benchmark of 10.29 per cent for 2017. The development in M2 is largely due to the contraction of 37.50 per cent in other assets net (OAN). Similarly, M1 contracted by 7.79 per cent (annualized to -9.35 per cent). Net domestic credit (NDC) expanded by 1.18 per cent, annualized to 1.42 per cent, driven primarily by net credit to government, which also expanded by 7.60 per cent against the programmed growth of 33.12 per cent. Credit to the private sector, however, contracted by 0.24 per cent in October 2017, compared with the provisional benchmark of 14.88 per cent. The MPC also noted the structural constraints in the transmission of credit to the real sector of the economy as well as the rising unemployment level. The Committee urged the Management of the Bank to continue to encourage the deposit money banks to accelerate the rate of credit growth to the real sector of the economy.

Inflationary pressures in the economy continued to moderate with headline inflation (year-on-year) receding for the ninth consecutive month to 15.91 per cent in October 2017 from 15.98 per cent in September 2017. Food inflation fell marginally to 20.31 per cent from 20.32 per cent in September, while core inflation increased slightly to 12.14 per cent from 12.12 per cent during the same period. These developments were attributable to the contraction in money supply, favourable but dwindling base effects, and the relatively stable naira exchange rate. In spite of the marginal decline in food inflation in October, the Committee noted that the rate remained high, traceable to cross border sales, distribution bottlenecks, high prices of farm inputs and supply shortages.

Money market interest rates oscillated in tandem with the level of liquidity in the banking system as the average inter-bank call rate, which opened at 12.00 per cent on October 3, 2017, closed at 5.38 per cent on November 16, 2017. The OBB rates opened at 10.41 per cent and closed lower at 6.02 per cent in the same period. However, the average inter-bank call and OBB rates for the period stood at 10.94 and 10.15 per cent, respectively. The development in net liquidity positions and flows reflected the effects of Federation Account payments to states and local governments; remittances by the Nigerian Customs, Federal Inland Revenue Services; OMO sales; foreign exchange interventions and maturing CBN Bills.

The Committee noted the continuing improvement in the level of external reserves and the equities segment of the capital market. External reserves grew to US$34.9 billion at the close of business on November 16, 2017. Similarly, the All-Share Index (ASI) rose by 3.38 per cent from 35,504.62 on August 31, 2017 to 36,703.58 on November 17, 2017. Market Capitalization (MC) improved by 4.35 per cent to N12.77 trillion from N12.24 trillion during the same period. Relative to end-December 2016, capital market indices rose by 36.57 and 38.10 per cent, respectively, indicating rising investor confidence, due to improvements in foreign exchange supply.

Total foreign exchange inflow through the central bank declined by 6.61 per cent in October 2017, compared with the previous month and attributable to the decline in crude oil and gas receipts as well as revenues from petroleum profit tax (PPT) and royalty payments. Total outflows, however, increased by 18.77 per cent during the same period, as a result of interbank sales, direct payments and JVC calls.

The Committee noted the gradual convergence between the rates at the bureau-de-change (BDC) and the Nigeria Autonomous Foreign Exchange (NAFEX) market segments, as well as the stability of the exchange rate at the inter-bank segments of the foreign exchange market during the review period. Similarly, the Committee viewed with satisfaction, the growing patronage at the Investors' and Exporters' (I&E) window of the foreign exchange market and attributed the development to increased confidence by foreign investors and the preference of Nigerian investors' and exporters' for the window compared with all other windows. The MPC noted that the I&E window had increased liquidity and boosted confidence in the market with over US$18.70 billion in transactions since its introduction in April 2017.

2.0. Overall Outlook and Risks

Forecasts of key macroeconomic variables indicate a positive outlook for the economy up to Q1 2018. This is predicated on continued implementation of the 2017 budget into early 2018, anticipated improvements in government revenue from the implementation of the Voluntary Asset and Income Declaration Scheme (VAIDS) as well as favourable crude oil prices. The development finance initiatives by the CBN in the real sector, particularly in agriculture, are expected to continue to yield positive results in terms of output expansion and job creation. Focusing on the downside risks to the outlook, the Committee noted the low fiscal buffers and weak aggregate domestic demand. On the external front, widening global imbalances, and rising geo-political tensions were some of the crucial risks identified.

3.0. The Considerations of the Committee

The Committee noted with satisfaction the second consecutive quarterly growth in real GDP following five quarters of contraction. In addition, Members welcomed the relative stability in the exchange rate, particularly the narrowing premia and the very slow deceleration in consumer price inflation, largely attributable to base effects. Overall, the economy has begun to show strong signs of recovery as public investment has picked up with increased housing construction at the Federal and state levels, as well as shipping activities at the ports. The Committee was, however, of the view that policy makers must not relent in their aggressive policy initiatives aimed at continuing the positive growth trajectory. The Committee was also concerned about potential adverse external developments and the cautious approach to lending and financial intermediation by domestic deposit money banks.

The Committee similarly evaluated other concerns in the domestic economy and the opportunities for strengthening output recovery, noting that some highly critical subsectors were yet to resume growth. The Committee noted the significant contribution of food prices to headline inflation and observed that the benefit of base effect on overall headline inflation had substantially dwindled. Members, however, expressed confidence that the tight stance of monetary policy and the stability in the exchange rate of the naira should continue to positively weigh in on price developments. The Committee reaffirmed its commitment to maintaining price stability, which is crucial to sustainable economic growth and development.

The Committee welcomed the review of the Economic Recovery and Growth Plan (ERGP), in an effort to realise the objectives of the plan. In the same vein, the Committee urges a quick passage of the 2018 Appropriation Bill by the National Assembly, so as to keep fiscal policy on track and deliver the urgently needed reliefs in terms of employment and growth of the economy.

On financial stability, the Committee noted the concentration of non-performing loans in a few sectors but observed that the overall condition and outlook for the banking system was stable as deposit money banks' balance sheets remained strong. This assessment is strengthened by developments in the national accounts and the expectations that the affected sectors are returning to growth. Nonetheless, the Committee urged further strengthening of supervisory oversight and deployment of early warning systems in order to promptly identify vulnerabilities and proactively manage emerging risks in the banking system. The Committee further observed that government was increasing debt, both domestically and externally, thus crowding out the private sector.

4.0. The Committee's Decisions

In arriving at its decision, the Committee appraised potential policy options in terms of the balance of risks. The Committee also took note of the gains made so far as a result of its earlier decisions; including the stability in the foreign exchange market and the moderate reduction in inflation and thus extensively deliberated the options regarding whether to hold, tighten or ease the policy stance.

While tightening would strengthen the impact of monetary policy on inflation with complementary effects on capital inflows and exchange rate stability, it nevertheless could also potentially dampen the positive outlook for growth and financial stability. On the other hand, whereas loosening would strengthen the outlook for growth by stimulating domestic aggregate demand through reduced cost of borrowing, it could aggravate upward trend in consumer prices and generate exchange rate pressures. The Committee also feels that loosening would worsen the current account balance through increased importation. On the argument to hold, the Committee believes that key variables have continued to evolve in line with the current stance of macroeconomic policy and should be allowed to fully manifest. Members noted that the developments in output and inflation in particular required effective close monitoring in order to gain clarity on the medium term optimal path of monetary policy.

In consideration of the foregoing, the Committee decided by a vote of 8 to 1 to retain the Monetary Policy Rate (MPR) at 14.0 per cent alongside all other policy parameters. One member voted to reduce the MPR by 100 basis points.

Consequently, the MPC voted to:

(i) Retain the MPR at 14.0 per cent;
(ii) Retain the CRR at 22.5 per cent;
(iii) Retain the Liquidity Ratio at 30.0 per cent; and
(iv) Retain the Asymmetric corridor at +200 and -500 basis points around the MPR.

Thank you for listening.

Godwin I. Emefiele
Governor, Central Bank of Nigeria
21st November, 2017