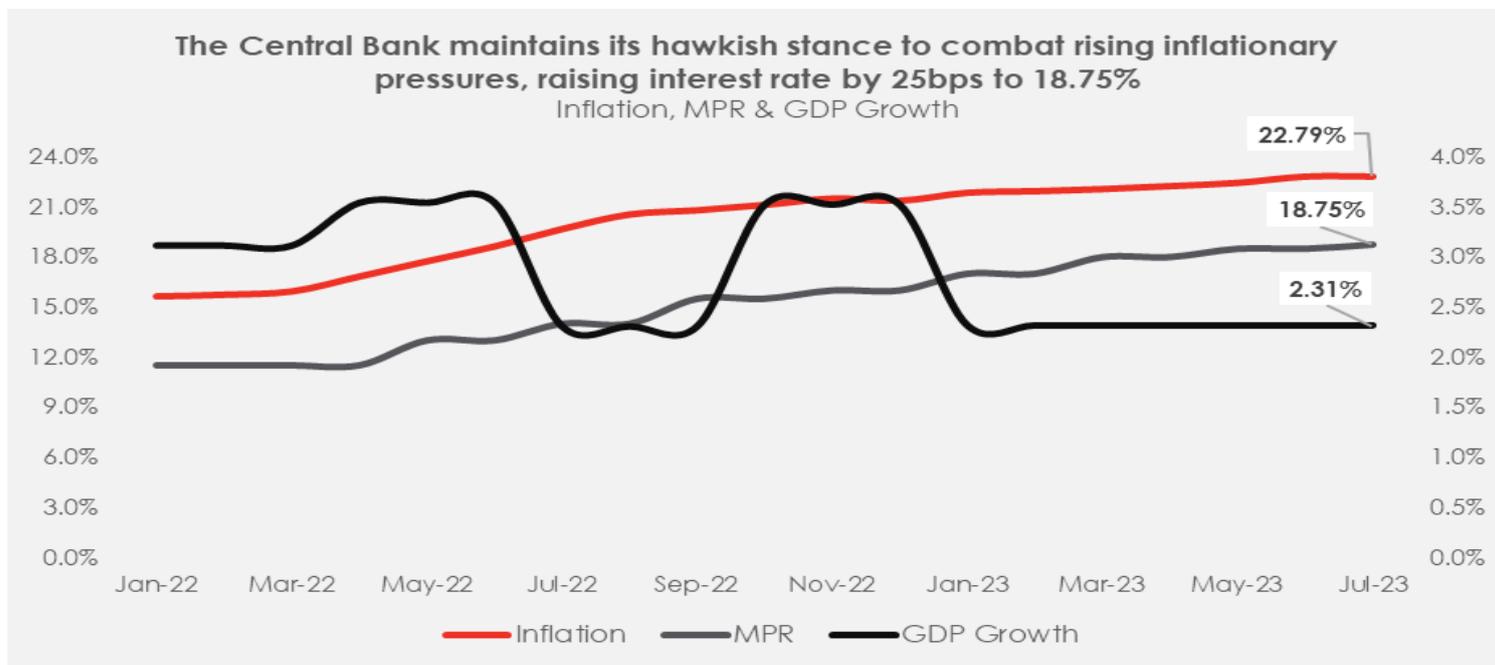


Flash Note

# Post MPC Note: Hawkish Monetary Policy Tone Persists

In its July 2023 meeting, the Monetary Policy Committee (MPC) concluded with a decision to raise the Monetary Policy Rate (MPR) by 25 basis points (bps) to 18.75% from the previous rate of 18.50%. The decision was supported by four members of the committee, while the remaining two members leaned towards a higher 50bps hike. Additionally, the MPC voted to adjust the asymmetric corridor around the MPR to +100/-300 basis points from the previous range of +100/-700 basis points. The committee also made the decision to retain the Cash Reserve Ratio (CRR) at 32.5% and the liquidity ratio at 30.0%.



Source: CBN, NBS, United Capital Research

The latest increase marks the fourth consecutive rate hike in 2023, amounting to a total cumulative rise of +725 basis points since May 2022. The decision was made by the Committee to persist in their efforts to combat inflation, acknowledging its potential impact on economic growth. They emphasized the effectiveness of previous rate hikes in slowing down the pace of rising prices, as well as the expectation of ample liquidity and its influence on future inflation trends. In making the final decision, the Committee carefully balanced the necessity to control inflation with the importance of supporting economic recovery through investments. As a result, they opted for a moderate rate hike to stabilize inflation, narrow the negative real interest rate gap, and foster increased investor confidence.

Looking ahead, the decision to hike rates is not expected to have a significant impact on inflation, as it is driven by cost-push factors. Instead, inflation numbers are likely to be influenced by activities in the foreign exchange (FX) market. The persistently high double-digit inflation will continue to hinder economic growth, remaining well above the 9.0% ceiling. In the financial markets, the ample system liquidity is anticipated to keep yields low. Consequently, a bearish outlook on yields necessitates a shift in fixed-income strategy. Our projections indicate limited opportunities in the fixed-income market for the remainder of the year. Market conditions are more favorable for long-term bond holders, as yields are floored, leaving room for buy-and-hold investors. However, significant sell-offs are improbable since rates at the short-end of the yield curve already hover at low single digits, while the average yield on FGN bonds stands at 12.7%, well below the inflation rate.

Fixed income securities continue to post negative real returns.  
Real returns (%)



Source: FMDQ, NBS, United Capital Research

However, due to the increasing negative real returns on fixed-income instruments and the ongoing foreign exchange crunch in the economy, it is unlikely that Foreign Portfolio Investors (FPIs) will resume investments in the Nigerian fixed income market. For fund managers and investors with a focus on equities, a different strategy is recommended. The decision of the Monetary Policy Committee (MPC) is not expected to cause a slowdown in equities in the short term. Additionally, a bullish corporate earnings performance in Q2-2023 and lower fixed-income yields are anticipated to trigger the usual asset rotation seen during a significant decline in interest rates. These factors are expected to provide strong support for Nigerian equities, leading to a favorable market performance.

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