

September 2024 Post MPC Note

# Policymakers Tightened with +50bps HIKE in Monetary Policy Rate

*The Key Fundamentals Behind the Committee's +50bps MPR Decision...*

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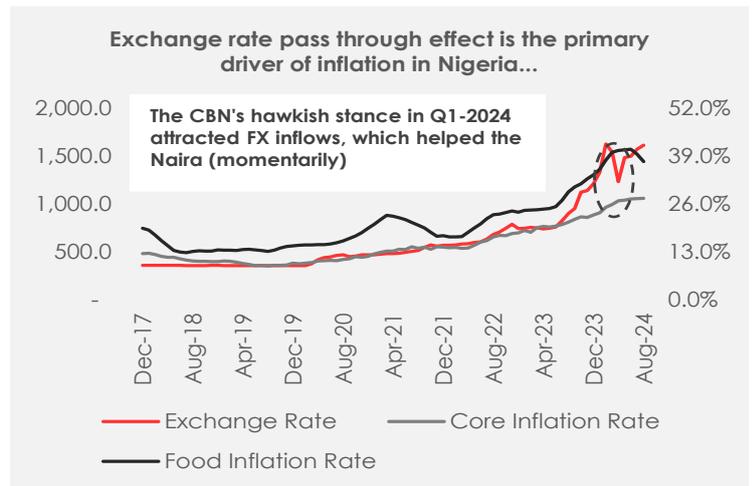
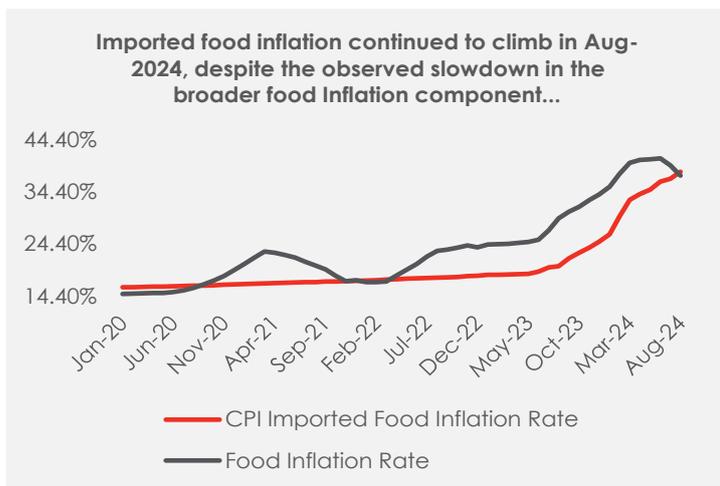
The 297th Monetary Policy Committee (MPC or the Committee) meeting held on 23 and 24 Sept-2024 saw a hike in Monetary Policy Rate (MPR or benchmark interest rate). The benchmark interest rate was increased by another +50bps from 26.75% to 27.25%. Notably, the banks were not spared, as the MPC also tightened the Cash Reserve Ratio of the banks. For the commercial banks, the Committee expanded CRR by +500bps from 45.0% to 50.0%, while CRR for merchant banks was raised by +200bps from 14.0% to 16.0%. Other monetary policy tools were left unchanged. For instance, the Liquidity Ratio was retained at 30.0% and Asymmetric Corridor stable at +500/-100 basis around the MPR).

### Key Fundamentals Behind the Committee's Decision

#### ⇒ Low Confidence in the Continuance of Recent Progress of Inflation:

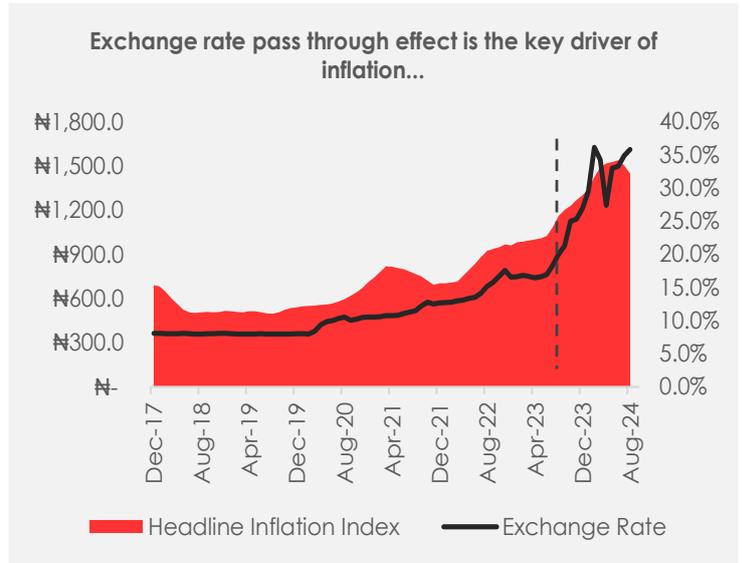
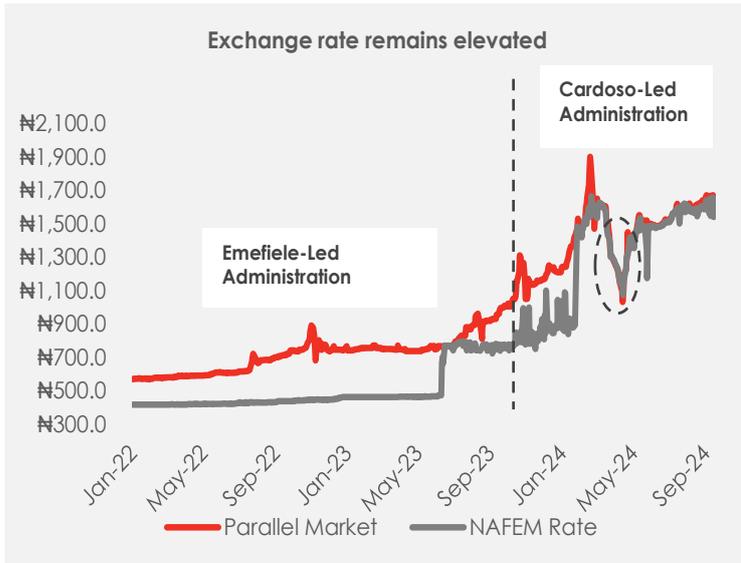
The CBN Governor, Mr. Olayemi Cardoso indicated the Committee's low confidence in the continuance of recent progress observed in inflation figures reported. Nonetheless, the Governor acknowledged the efficacy the recent monetary policies actions, stating that "the numbers clearly show we are in the right direction". Recently, the National Bureau of Statistics (NBS) revealed that the Nigeria's headline inflation printed at 32.15% on a year-on-year (y/y) basis in Aug-2024, indicating a 125bps reduction from 33.40% y/y in Jul-2024. Notably, this marked the second successive month of slowdown on a year-on-year basis. Particularly, this was driven by the decline in food prices, supported by harvest period and fiscal interventions (150 days duty-free import window for select food items).

### The Committee's Key Concerns



Sources: NBS, FMDQ, United Capital Research

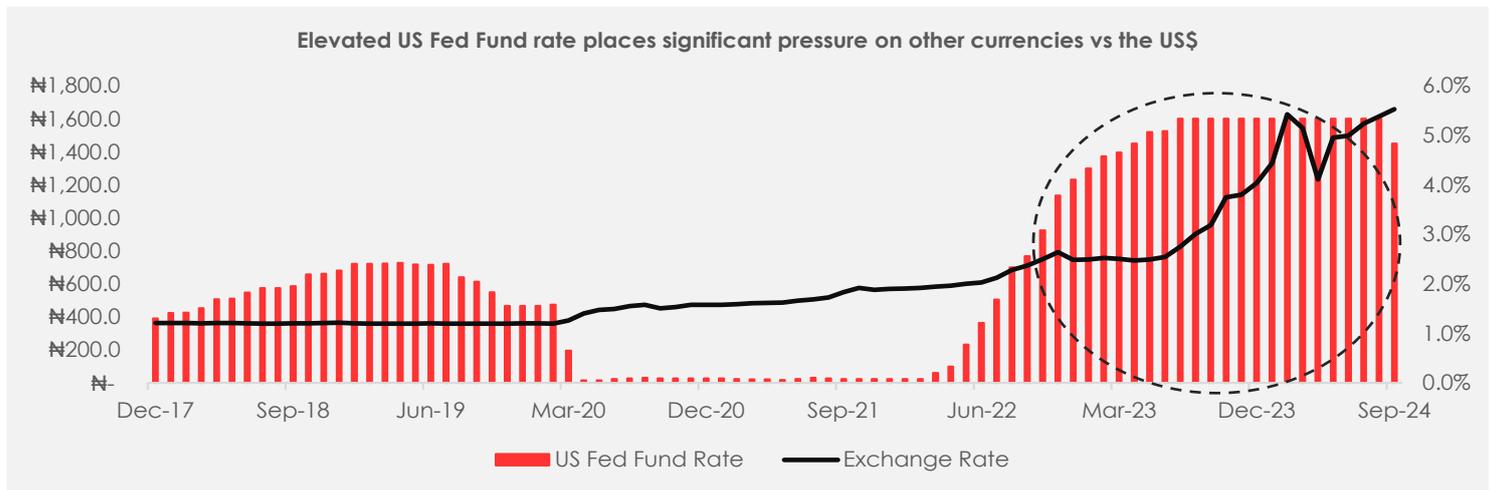
⇒ **Exchange Rate Passthrough Effect:** The Committee's position of a 50bps hike emanated from the extensive pressure resulting from an elevated exchange rate. Pass through effects from the elevated exchange rate environment continued to stand as a stubborn tailwind for core inflation rate and imported food inflation rate, which continued to climb in August 2024.



Sources: FMDQ, NBS, United Capital Research

- ⇒ **The Recent Hike in Fuel Prices:** Petrol pump prices spiked in the first week of September, climbing by approximately 65.0%, from around N579.50 – 625.0/litre to N855.00 – N978.00/litre. This period was also marked with unrepresented scarcity as evidenced by long queues, emanating to black market activities where petrol price printed at N1,100 – 1,500/litre. Consequently, the Committee envisaged that the factor could cause a strain in inflation progress (particularly on the core inflation component). However, Dangote Refinery which is anticipated to reduce petrol imports, slash gas pump prices, and improve gasoline supply stability, is the glimmer of hope to counteract this factor. This is especially relevant given the new arrangement wherein NNPC sells crude oil to local refineries (incl. Dangote Refinery) in Naira (and vice versa).
- ⇒ **Nigeria's Heavy Dependence on FX (US\$) Proceeds from Crude Exports:** The Committee advocated for economic diversification which may result in the expansion of the non-oil sector. This entails improving the fundamentals of local costs of production, with the aim of disincentivising import dependence, and thus curbing the heightened demand for FX (US\$). In the same vein, the Committee highlighted that the lifting of refined petroleum products from the Dangote Refinery would create a significant buffer for the country's FX reserves by significantly shrinking the demand for FX (\$). Additionally, this may improve the country's ability to increase US\$ supply in the local economy, with the aim of defending the strength of the Naira. Ultimately, the Committee expressed optimism indicating that the lifting of refined petroleum products from Dangote Refinery would reduce transportation costs, curb inflation, and bolster the nation's foreign reserves. This is especially true under the Naira-for-Crude arrangement between NNPC and the Refinery.
- ⇒ **Positive Correlation between FAAC Payments and Exchange Rate Volatility:** Additionally, the Committee looked to address exchange rate volatility emanating from FAAC payments.

⇒ **Global Monetary Policy Easing:** In Sept-2024, the Federal Open Market Committee (FOMC) cut its key overnight borrowing rate by 50 basis points, or half a percentage point, in response to signs of slowing inflation and a weakening labour market. Notably, this is the first interest rate cut since the early days of COVID-19 pandemic. To put this in context, interest rate cuts by the U.S. Federal Reserve typically result in a weakening of the U.S. Dollar due to a number of factors, including lower interest rates on assets denominated in Dollars, increased money supply (which stems from increased consumer credit), and capital outflows (as investors seek higher returns abroad in countries offering more favourable rates). Ultimately, as capital moves out of the U.S., the demand for Dollars declines, which can in turn weaken the U.S. Dollar. The Naira is well-positioned to appreciate in value as a result of the Committee's decision to raise MPR by +50bps. This could potentially mitigate the predominant exchange rate pass-through impact, which has become the primary driver of the inflation rate.



Sources: Bloomberg, FMDQ, United Capital Research

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