NESG MPC Alert

January 2021

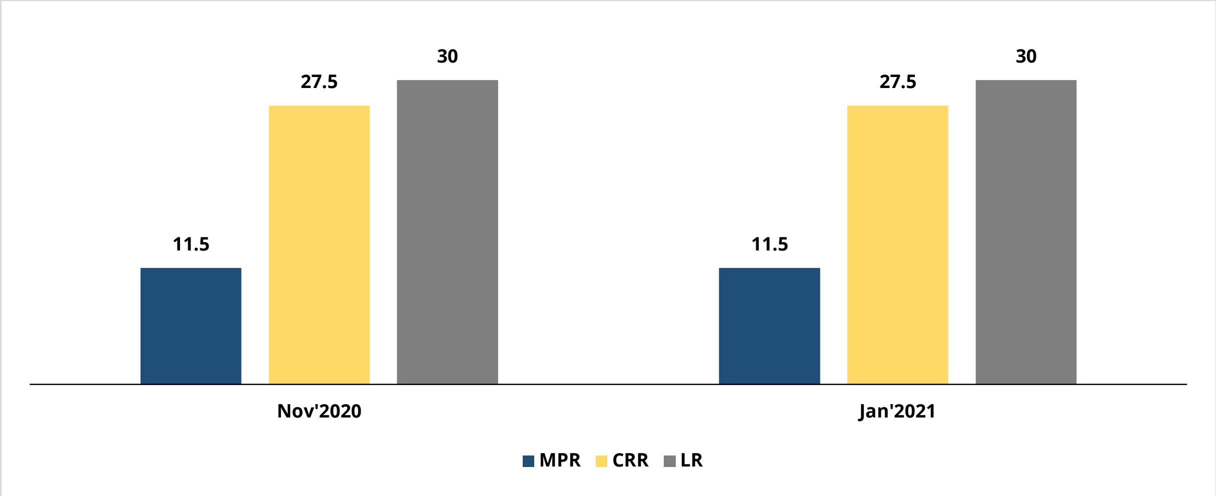
MPC maintains status quo amid the outbreak of a new strain of COVID-19

The Central Bank of Nigeria (CBN) Monetary Policy Committee (MPC) held its first meeting for the year 2021 on January 25-26. At the meeting, the committee members unanimously voted to keep all monetary policy parameters unchanged as follows:

- Monetary Policy Rate at 11.5%;
- Cash Reserve Ratio (CRR) at 27.5%;
- Liquidity ratio at 30% and an asymmetric corridor of +100/-700 basis points around the MPR.

The decision represents the second consecutive session that the committee members would maintain status quo on all monetary parameters (see **Figure 1**)[1]. The MPC members met at a time when the Nigerian economy is battling with the recurrence of stagflation - which is a combination of rising inflation and output contraction – as was witnessed during the 2016 recession.

Figure 1: Trend of monetary policy parameters (%)



Source: Data: CBN; Chart: NESG Research.

Meanwhile, having weighed the benefits associated with the retention of monetary policy parameters against the costs associated with easing or tightening monetary policy, the MPC adjudged the current stance as appropriate considering the multiplicity of fiscal and monetary stimulus packages that are being deployed to reverse the recession. The MPC also acknowledged the potency of the 65% Loan-to-Deposit Ratio (LDR) policy as reflected in a quicker growth in aggregate domestic credit at 13.4% in December 2020 from 9.5% in the previous month. The policy has, however, not undermined the quality

[1]Though at different levels of the benchmark interest rate, the MPC has previously held all monetary parameters unchanged in March and July 2020.

of banking assets with the relative stability of the non-performing loan ratio within the range of 5%-6.7% since the LDR was adjusted to 65% from 60% in December 2019.

Concluding Remarks

The monetary policy environment was highly constrained in the year 2020 to the extent that a cumulative interest rate cut of 200 basis points could not save the economy from slipping into its second recession in a space of 5 years. While there is improved prospect of a global economic recovery on the backdrop of mass production and distribution of COVID-19 vaccines, the Nigerian government has a herculean task to implement key structural reforms that would make the economy not only to exit recession, but also come out strong and become resilient against global shocks going forward.

Though the CBN would deploy its traditional instruments including OMO Bill and the recently introduced Special Bill to manage excess liquidity, key factors, such as, the deregulation of the downstream oil sector, VAT increase, market-reflective electricity tariff and heightening insecurity would keep inflation elevated going into 2021. This, therefore, requires the need for a policy coordination between the fiscal and monetary authorities considering the inevitable trade-off between inflation and economic growth. In addition, the key economic fundamentals that would influence the direction of monetary policy in 2021 include the nature of global and domestic economic conditions, external reserves position, crude oil prices and inflation.

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