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Nigeria | Macroeconomics

Ahead Of MPC Report

September 2024

Committee Set to Hold its Fifth Meeting in 2024

MPC poised to adopt accommodative stance amidst easing inflationary trends

The Monetary Policy Committee (MPC) is set to hold its fifth meeting of the year on September 23rd and 24th, 2024.

At this meeting, we expect the MPC to consider several key factors, including disinflationary trends in advanced economies, the recent 50bps rate cut by the US Federal Reserve, global economic growth patterns, the recent decline in oil prices, and the possible repercussions of these developments on Nigeria's economy.

In August, Nigeria's inflation rate declined for the second consecutive month, falling to 32.15% YoY from 34.19% YoY in July 2024. The decline was mainly driven by a drop in food prices, attributed to a higher supply from the harvest season. However, core inflation rose to 27.58% YoY (vs 27.47% in July), hinged on increased transportation costs resulting from the fuel scarcity that began in August 2024.

Furthermore, the steady foreign reserves and successful domestic dollar-denominated bond issuance indicate the Central Bank of Nigeria's (CBN) capacity to provide sufficient liquidity to the exchange rate market in the short term, supporting the MPC's exchange rate management objective.

Overall, we expect the committee to consider the anticipated stability in food prices, which could affect inflation in the near term, along with the need to address rising borrowing costs while carefully monitoring capital inflows into the economy. As a result, we anticipate that the MPC will opt for a rate hold while maintaining other parameters to effectively meet these objectives and maintain economic stability.

Committee’s Expected Decision

On a Balance of Factors…

We expect the Committee to:

- **Maintain MPR at 27.25%**
- **Retain Liquidity Ratio at 30%**
- **Retain the Asymmetric Corridor at +500bps/-100bps around the MPR.**
- **Maintain the CRR at 45.00%**

International Economies and Developments

Inflation and Monetary Policy

Inflation Declines Further Prompting Easing Cycle by Major Central Banks

Globally, inflation continues to trend downward, with notable improvements in key economies. In the US, headline inflation eased to 2.50% in August 2024, down from a marginal rise to 2.90% in July. Similarly, inflation in the Eurozone fell to 2.20% in August, compared to 2.60% the previous month. Meanwhile, the UK's inflation rate held steady at 2.20% in August, unchanged from July. These inflationary declines can largely be attributed to lower food prices, stabilized energy costs, and improved supply chain conditions, alongside reduced demand pressures.

In response to these developments, central banks have adopted a more dovish approach. The European Central Bank (ECB) cut interest rates by 30bps to 3.50%, marking its second consecutive rate reduction in 2024. The US Federal Reserve followed suit, reducing rates by 50bps — its first rate cut in four years — reflecting a favourable shift in key economic indicators. **With inflation cooling and labour markets showing signs of stability, we anticipate that major central banks will maintain their dovish monetary policy stance in the near to medium term.**

Global Growth

Economic Recovery Continues in the Global Scene

Recent data has shown varied growth trajectories among global economies in Q2:2024. The US economy expanded by 3.00%, up from 2.80% in the same quarter the previous year, propelled by robust government and consumer spending. The UK also saw its GDP rise by 0.90% in Q2:2024, a rebound from stagnation in the prior period, primarily driven by increased government and household expenditure and a 0.80% YoY growth in the services sector, which constitutes c.79% of the total GDP.

Meanwhile, in the Eurozone, GDP growth accelerated to 0.60% in Q2:2024 from 0.50% in Q2:2023, marking the strongest performance since Q3:2023. This growth was fuelled by resilience in major economies like Germany and favourable trade dynamics within the region. In contrast, China's growth decelerated to 4.70% YoY in Q2:2024 from 6.30% in Q2:2023, hampered by subdued consumer spending amid job security fears and low consumer confidence. The ongoing decline in property values continues to exert pressure on China's economic performance. Moving forward, a shift in focus towards stimulating growth is anticipated across these major economies.

Oil Prices Rebound Amid Demand Uncertainties

Global oil demand growth was revised downwards by the OPEC+ to 2.03 million barrels per day (mbpd), a reduction from the 2.11mbpd forecast in August. Projections for 2025 were also scaled back to 1.74mbpd. This downward adjustment reflects expectations of reduced oil consumption, primarily driven by China's ongoing economic challenges and the global shift towards cleaner energy alternatives. On the supply side, OPEC+ opted to delay plans for increased oil production in an effort to maintain price stability in the market. After a significant dip in prices earlier in the month, both West Texas Intermediate (WTI) and Brent Crude saw recoveries, with WTI rising by 6.28% to USD69.88 per barrel 9pb) and Brent Crude gaining 5.33% to settle at USD72.88pb.

In light of these market developments, we anticipate that the Monetary Policy Committee (MPC) will weigh these global oil trends and their potential impacts on inflation and economic stability in its upcoming policy decisions.

Domestic Macros

Economic Growth

Growth Boosted by Oil Gains While Non-Oil Struggles Persist

As reported by the National Bureau of Statistics (NBS), Nigeria's economy grew by 3.19% YoY in Q2:2024, up from 2.51% YoY in Q2:2023 and 2.98% YoY in Q1:2024. This growth was primarily driven by a 10.15% YoY expansion in the oil sector (compared to 13.43% YoY in Q2:2023 and 5.70% in Q1:2024) and steady growth in the non-oil sector at 2.80% YoY (vs 3.58% in Q2:2023 and 2.80% in Q1:2024). The increase in the oil sector was fueled by higher oil production at 1.41mbpd (up from 1.22mbpd in Q2:2023) and a low base effect from Q2:2023.

Looking ahead, oil production is poised for a boost in the short to medium term. This outlook is hinged on several key factors, including the startup of production at the new Madu Field and the expected restart of operations at recently acquired terminals that have been dormant for quarters. Additionally, government initiatives to enhance security along oil infrastructure and the auctioning of oil blocks to new operators are expected to elevate overall production. August oil production average of 1.57mbpd (marking an eight-month high), reinforces this positive outlook.

The non-oil sector, on the other hand, continues to struggle with macroeconomic challenges, including high interest rates, continued Naira depreciation, and inflationary pressures, which have dampened output in several non-oil sub-sectors, such as manufacturing, agriculture, and telecommunications. However, sectors like financial services and insurance have posted strong performance, growing by 28.79% (compared to 26.84% in Q2 2023), contributing to the expansion of the non-oil sector during the period.

Considering that the challenges hindering substantial improvement in the non-oil sector are likely to persist in the near term, we anticipate the non-oil sector's moderate growth to continue, with sectors like financial services and insurance driving overall performance.

Therefore, we anticipate that the MPC will take into account the ongoing effects of previous policy decisions on the country's economic growth trajectory, prompting a cautious stance in its upcoming meeting.

Inflation

Inflation Rate Declines Again as Harvest Season Brings Relief

In August 2024, Nigeria's headline inflation rate to 32.15% YoY (from 33.40% YoY in July 2024), marking the second consecutive month of disinflation since December 2022. This decline was largely driven by a slowdown in food inflation, which eased to 37.52% YoY (compared to 39.53% in July). However, core inflation inched up to 27.58% YoY in August (from 27.47% in July 2024).

The drop in food inflation can be attributed to a high base effect from the previous period and increased supply of key staples during the ongoing harvest season, which led to softened prices for items like yam, rice, and tomatoes, reducing food price pressures.

On the other hand, the rise in core inflation was primarily driven by higher transportation costs due to the fuel scarcity that started in August 2024, overshadowing the relative stability of the Naira during the period.

Looking ahead, we expect food inflation to continue moderating in the near term, driven by increased supply of items like maize and soybeans from the ongoing harvest. Measures such as subsidized rice sales and an import duty waiver should also help ease cost pressures. However, rising transportation costs due to higher fuel prices and a waning base effect may partially offset these benefits. Additionally, we anticipate that the fuel price increases and fluctuations in the foreign exchange market will keep influencing core inflation in the coming months.

We anticipate that the MPC will take a cautious approach in light of the recent disinflation trend and the ongoing harvest season, which may stabilize food prices in the near term. Moreover, the potential for a higher core index due to rising fuel prices minimizes the likelihood of a rate cut in the upcoming meeting.

Fiscal Policy

Fiscal Policy

Growing Implications for Widening Debt

Following the MPC meeting in July, several key developments have emerged in Nigeria's fiscal landscape. The Debt Management Office (DMO) successfully raised USD500mn through a dollar-denominated bond, contributing to a higher national debt burden. In parallel, the Central Bank of Nigeria (CBN) has reaffirmed its policy of maintaining a 5% cap on Ways and Means advances to the government, stressing the need to repay these advances within the fiscal year to avoid further long-term debt obligations. With the recent influx from the bond issuance and additional funding expected through multilateral loans and domestic borrowings to cover budget shortfalls and government expenses, Nigeria's debt levels are likely to rise even further. The combination of external borrowing and domestic fiscal measures highlights the government's need for continued fiscal discipline and strategic debt management to avoid worsening the country's financial position.

Harmonizing Growth and Progress

The fiscal authority has implemented several measures to boost government tax revenue, including the reintroduction of a 0.005% cybercrime levy on all electronic transactions as outlined in the CBN's 2024-2025 Monetary, Credit, Foreign Trade, and Exchange Policy Guidelines. This is part of a broader effort to strengthen revenue generation.

In the light of tax revenue performance, the NBS reported a modest 9.11% increase in Value Added Tax (VAT) revenue, which grew to NGN1.56trn in Q2:2024 from NGN1.46trn in Q1:2024. Of the total VAT collected, NGN792.58bn came from local payments, NGN395.74bn from foreign VAT, and NGN372.95bn from import VAT. Meanwhile, revenue from Company Income Tax (CIT) surged to NGN2.47trn in Q2:2024, marking a significant 150.83% increase from NGN984.61bn in the previous quarter.

Despite these revenue gains, government expenditure is expected to rise in response to recent challenges. The devastating floods that impacted agricultural farmlands, particularly in the Northeastern food-belt states, threaten food security. Consequently, the government's efforts to provide relief materials to the affected regions are expected to increase short-term public spending. Additionally, further strain on government expenditure is anticipated from various initiatives such as the distribution of fertilizers and tractors to farmers, the recently approved 50% electricity subsidy for public hospitals and tertiary institutions, and the sale of 50kg bags of rice at subsidized rates to civil servants. These welfare programs, while essential, are likely to exert further pressure on the government's fiscal balance in the near term.

Government spending is projected to increase in the near term, driven by expansionary fiscal policies aimed at enhancing the living standards of citizens, alongside the growing burden of debt servicing. While efforts to improve tax revenue collection and anticipated VAT hikes are underway, the suspension of import levies on essential agricultural commodities may offset these gains, leading to a potential shortfall in overall government revenue in the near term.

Monetary

Monetary Policy

A Balancing Act

At its last meeting, the MPC raised the MPR by 50bps to 26.75%, up from 26.25%, and adjusted the asymmetric corridor to +500/-100bps from +100/-300bps. The Committee also maintained the Cash Reserve Ratio for deposit money banks at 45% and merchant banks at 14%, while keeping the liquidity ratio unchanged at 30%. Investors and stakeholders are now watching closely to gauge the impact of these changes on market yields, foreign capital inflows, and the financial markets.

The country's foreign reserves have appreciated slightly to USD37.39bn MtD. However, on a YtD basis, the increase has been more significant, rising by 13.62%. This movement comes amid a dip in crude oil prices, with Brent crude averaging USD76.18 per barrel so far this month, down from USD85.06 per barrel during the last MPC meeting. The decline in oil prices is largely attributed to concerns over weakening demand from China and increased production from OPEC+ nations.

Following the meeting, the Naira depreciated to NGN1,617.08/USD but later appreciated to NGN1,541.52/USD, driven by the DMO's issuance of USD500.0mn in domestic dollar-denominated bonds, which attracted strong demand with subscriptions totalling USD900.00mn. However, a renewed divergence between the official and parallel markets has emerged, with the premium of the parallel market over the official rate widening to NGN103.48/USD — the first time this gap has been seen since February 2024.

Money market activities have largely mirrored the CBN's revision of the asymmetric corridor and the newly imposed NGN3bn cap on the Standing Deposit Facility (SDF). This policy shift has led to a decline in short-term interest rates, with Open Buy Back (OBB) and Overnight rates now standing at 29.69% and 29.97%, respectively, compared to 34.88% and 35.53% during the previous MPC meeting.

As such, we anticipate that the monetary authorities will maintain a hold stance, due to the moderating inflation rate, the need to manage money supply issues, and keep capital inflows at an attractive level.

Markets

Fixed Income Market

Torn Between Cost & Monetary Control

Following the MPC's decision to raise the benchmark interest rate by 50bps to 26.75% at its last meeting, yields in the fixed income market rose in tandem. This was reflected in the Primary Market Auction (PMA) for Treasury bills on July 24, where stop rates on the trio instruments – 91-day, 182-day, and 364-day instruments climbed from 18.49%, 19.29%, and 21.89% to 18.50%, 19.50%, and 22.10%, respectively. However, by August, yields began to taper due to reduced government borrowing requirements and increased demand, spurred by improved system liquidity, which peaked at NGN274.82bn. Additionally, the MPC's adjustment to the asymmetric corridor in August led to revisions in the SLF and SDF rates to 31.75% and 25.75%, respectively, with a NGN3bn cap on the SDF. Consequently, banks were disincentivized from using the CBN's deposit facility, as demonstrated by the lower SDF placements, which stood at NGN5.48trn, compared to the higher SLF uptake of NGN7.75trn during the same period.

As a result, rates in the Treasury Bills Primary Market Auction fell during the period, with the trio instruments dropping to 16.63%, 17.00%, and 18.59%, respectively, (vs 18.49%, 19.29%, and 21.89% prior to the last MPC meeting). Likewise, longer-term bond yields in the PMA saw a downward shift, with the 7-year and 9-year bonds now at 20.90% and 21.50% (vs 21.00% and 21.98% from the previous auction). However, the rate on the 5-year bond rose to 20.30%, up from 19.89% in July, largely driven by increased demand and lower allotments, resulting in a bid-to-cover ratio of 1.23x in August. During the period, a five-year domestic dollar bond was introduced, offering a 9.75% coupon. The auction attracted significant interest, with an oversubscription of USD900mn —80% above the initial issue size of USD500mn. This strong demand highlights growing investor confidence, particularly among those holding dollars, which is positive for the attainment of a more stable exchange rate.

Contrarily, mixed sentiments dominated the secondary market since the last meeting, as the average T-Bills yields declined to 20.28% (vs. 24.84% at the last meeting) while the average bonds yields rose to 18.84% (vs. 17.50% as at the last meeting).

We anticipate the MPC will take a dovish stance in its upcoming meeting, driven by lower borrowing needs as alternative funding sources are utilized and a focus on managing borrowing costs.

Equities Market

Bearish Bias Prevail Amid Wavering Sentiments

Investors' appeal towards equity assets waned further since the last MPC meeting. Evidently, the market recorded negative returns in July and August (-2.25% and -0.80%, respectively). This was driven majorly by sell-offs on some bellwether stocks like **MTNN** (-3.90%) and **NESTLE** (-3.26%), coupled with profit-taking activities on **DANGCEM** (-18.99%) and **BUACEMENT** (-20.46%). Thus, the NGX-ASI settled at 99,768.64pts. Meanwhile, September has been characterized by improving sentiment, as the market recorded an uptick of +1.73% MtD as of 20th September.

Across sectors, the performance was predominantly positive as **NGXOILGAS** (+28.24%), **NGXINS** (+8.84%), **NGXBNK** (+6.17%), **NGXCNSMRGS** (+0.95%), and **MERI-AGRIC** (32.35%) all recorded gains. However, **NGXINDUSTR** (-18.21%), and **MERI-TELCO** (-0.94%) closed in the red zone. The upbeat sentiment in these sectors was fueled by key corporate actions (such as Zenith Bank's right issue and FCMB capital raise), and **OANDO's** acquisition of Agip Oil company. On the other hand, poor financial results and UCAP's stock split dampened the broader market performance.

From our analysis, activities in the market have primarily been driven by corporate disclosure across sectors since the last MPC meeting. Moreover, investors' risk-off bias has largely eased due to the declining yields in the fixed-income market. *While we expect the activities of the equities market to loosely influence the MPC's decision, we opine that a less hawkish stance will likely spur investors' appetite for equity assets.*

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