MERISTEM

Nigeria | Macroeconomics

Post MPC Report

November 2024

Monetary Policy Moves: MPC Takes a Cautious Step Forward

At its 298th Monetary Policy Committee (MPC) meeting held on November 25th and 26th, 2024, the MPC deliberated on pivotal choices to guide monetary policy route. The Committee decided to raise the Monetary Policy Rate (MPR) by 25bps from 27.25% to 27.50%. Other key parameters were left unchanged: the Cash Reserve Ratio (CRR) for Deposit Money Banks and Merchant Banks remains at 50.00% and 16.00%, respectively, the Liquidity Ratio at 30.00%, and the asymmetric corridor at +500 basis points/-100 basis points around the MPR.

On the global scene, the MPC considered the slowdown in global inflation, with the deceleration trend expected to continue into 2025. However, factors including ongoing geopolitical tensions (Russia-Ukraine war & the Middle East crisis) and the potential impact of the incoming Trump administration on trade dynamics, pose potential reversal risks to inflation trend.

For the domestic economy, key considerations encompassed the renewed uptrend in inflation as the headline, food, and core inflation rose YoY and MoM in October 2024, suggesting persistence price pressures. The committee also noted fiscal efforts to improve security in the northeast, which could boost food production. Additionally, the MPC highlighted improvement in the external sector on the back of enhanced remittance, increased capital inflows, and current account surplus position, indicating that key monetary and fiscal policy measures are beginning to yield desired outcomes. The MPC emphasized the resilience of the banking system and its robust financial indicators, encouraging the CBN to continue its oversight efforts to uphold the financial system's stability.

However, the MPC expressed concerns about persistent exchange rate pressures stemming from heightened demand in the FX market and reaffirmed its dedication to curbing inflation and ensuring price and exchange rate stability.

The MPC's ongoing tightening efforts to curb inflation and stabilize the FX market carry varying implications for the financial markets. Fixed-income yields are expected to remain elevated, with the latest rate hike likely having a more muted impact on treasury yields. Despite these policy adjustments, a significant capital shift from the equities market is unlikely, as investor sentiment is expected to remain guided by fundamentals.
The next meeting of the committee is scheduled to hold on the 25th and 26th of January 2024.

Committee's Decisions

In summary, the Monetary Policy Committee (MPC) opted to further tighten monetary policy as follows:

- Raised the benchmark rate (MPR) by 25bps to 27.50% from 27.25%
- Retained the Cash Reserve Ratio (CRR) of Commercial Banks at 50.00%.
- Retained the Cash Reserve Ratio (CRR) of Merchant Banks at 16.00%.
- Retained Liquidity Ratio at 30.00%.
- Retained the Asymmetric Corridor at +500bps/-100bps around the MPR.

MERISTEM

Anticipated Impacts

The Banking Sector

Banking on Elevated Rates

The Monetary Policy Committee (MPC) raised the MPR by 25bps, bringing the cumulative increase in 2024 to 875bps, with the rate now at 27.50%. This aggressive monetary tightening has broadly benefitted Nigerian banks, enabling them to capitalise on a high-interest-rate environment through upward loan repricing and improved yields on investment securities.

The recent hike is expected to maintain this momentum, with average lending rates, treasury bills rates, and bond yields increasing by 1709bps, 1726bps, and 528bps to 32.36%, 23.55%, and 19.41%, respectively, compared to 15.27%, 6.29%, and 14.13% at the close of December 2023. Banks are anticipated to continue leveraging these higher yields on fixed-income instruments, further boosting earnings. This trend is expected to translate into higher YoY interest income for our coverage banks in the upcoming 2024FY results, offsetting the rise in MPR-driven interest expenses. For context, industry-wide interest income rose by 147.58% YoY as of 9M:2024. However, the industry's current account & savings account (CASA) mix declined to 74.31% in 9M:2024 from 88.11% in H1:2024, indicating a reduction in cheaper deposit sources. Improving the CASA mix will remain critical for banks to bolster net interest margins and overall profitability.

Despite the CBN’s aggressive monetary tightening, the banking industry's capital adequacy, non-performing loans, and liquidity ratios remain at comfortable levels. It is noteworthy that the MPC's tone at the most recent meeting hinted at the possibility of a more accommodative stance in the near term. Banks are likely to intensify efforts to grow income from non-interest sources as part of their strategic focus.

Overall, while the MPC’s tight policy stance continues to support high yields, boosting banks' earnings through loan repricing and fixed-income investments, it also poses challenges to asset quality. As a result, banks must prioritize regulatory compliance and optimize funding structures to sustain profitability and resilience in the face of tighter monetary conditions.

The Real Sector

Subdued Real Sector Growth Likely to Persist

The Monetary Policy Rate (MPR), currently at 27.50% following a 25bps hike by the Monetary Policy Committee (MPC), is expected to further exert pressure on the real sector. This is evident in the fourth consecutive quarterly slowdown in growth across key sub-sectors. The manufacturing and real estate sub-sectors recorded decelerations to 0.92% YoY and 0.68% YoY in Q3:2024, respectively, compared to 1.28% and 0.75% in Q2:2024. Further underscoring the challenges, the Purchasing Managers' Index (PMI) averaged 49.63pts in Q3:2024, down from 51.10pts in Q2:2024, signalling contraction in manufacturing activities as it fell below the 50-point threshold.

Additionally, elevated borrowing costs and mounting financial obligations, coupled with ongoing macroeconomic challenges, are expected to further weigh on productivity and deter capital investments (capex) within the real sector. Nevertheless, the recent 25bps rate hike (the smallest adjustment under the current administration) could hint at a gradual shift toward a more accommodative monetary policy stance. This pivot holds the potential to alleviate financial and operational pressures on businesses in the near term, fostering a more supportive environment for economic activity.

In summary, while the rate hike is expected to support FX stability and sustaining foreign portfolio investments in the short term, its adverse effects on borrowing costs and will likely exacerbate financial stress on businesses. This could lead to subdued productivity and a further decline in real sector output for Q4:2024. Thus, we maintain a cautious outlook, anticipating gradual relief as monetary policy potentially softens in the medium term.

Anticipated Impacts

The Fixed Income Market

Persistently High Yields Driven by Liquidity Pressures

The recent 25bps hike in the MPR, though smaller in magnitude compared to prior increases, is expected to keep yields in the fixed income market elevated, continuing the trend of investor interest in these assets. However, given that liquidity remains a primary driver of yield direction, the effect of this latest hike on treasury yields is expected to be more muted. With system liquidity currently at NGN438.02bn as of November 26th, 2024, the market's responsiveness will largely depend on how these conditions evolve.

Additionally, the government's approach to debt management continues to influence the market significantly, with the recently released December issuance calendar reflecting higher paper supply (NGN1.39trn vs NGN1.32trn in November), aligning with expectations of increased borrowing to address fiscal pressures. In recent auctions, there has been a clear shift towards higher stop rates, signalling the government's readiness to accept increased borrowing costs. In the most recent bond and treasury bill auctions, average stop rates rose to 21.50% and 20.00%, respectively, compared to 21.25% and 19.83% in previous auctions.

This trend of rising MPR is likely to push borrowing costs for corporates higher, which could limit access to affordable short-term financing. This, in turn, may discourage corporate issuers from tapping the debt market unless absolutely necessary.

Investors should leverage the high-yield environment by focusing on the shorter-end of the yield curve for optimal returns while carefully monitoring liquidity trends and auction dynamics to strategically time their participation and manage risks.

The Equities Market

Mixed Sentiment to Persist Amid Cautious Trading

For the local bourse, we expect the 25bps hike to have a minimal impact on market activities. In our view, market participant's broad position to strategically capitalize on value opportunities and end-of-year portfolio adjustments would largely dictate market direction despite tighter monetary conditions.

As such, we foresee increased investor interest in sectors poised to benefit from a higher interest rate environment, particularly the financial services sector, as we have observed from recent market activities.

Conversely, the manufacturing sector, particularly consumer goods and industrial goods sectors may continue to face headwinds due to rising costs of borrowing, subdued consumer demand, and margin pressures, which could dampen earnings performance and weigh on investor confidence.

Meanwhile, according to data from the NGX, foreign inflows into the equities market increased by 195.83% MoM to NGN33.31bn in October, despite the previous hike in September. Thus, we do not anticipate a reversal in portfolio investment inflows into the equities market.

Nonetheless, we note that domestic investors continue to dominate market participation and may be influenced by movements in treasury yields. Thus, we do not overrule the possibility of occasional risk-off bias.

CONTACT INFORMATION

Brokerage and Retail Services
topeoludimu@meristemng.com (+234 905 569 0627)
adaezeonyemachi@meristemng.com (+234 808 369 0213)
contact@meristemng.com

Investment Banking/Corporate Finance
rasakisalawu@meristemng.com (+234 806 022 9889)
davidadu@meristemng.com (+234 810 940 4836)

Wealth Management
funmilolaadekola-daramola@meristemng.com (+234 803 355 0008)
crmwealth@meristemng.com (+234 01 738 9948)

Registrars
nkechinyeluokoye@meristemng.com (+234 803 526 1801)
www.meristemregistrars.com (+234 01 280 9250)

Group Business Development
ifeomaanyanwu@meristemng.com (+234 802 394 2967)
info@meristemng.com

Trust Services
damilolahassan@meristemng.com (+234 803 613 9123)
trustees@meristemng.com

Investment Research
praiseihansekhien@meristemng.com (+234 817 007 1512)
research@meristemng.com

Client Services
adefemitaiwo@meristemng.com (+234 803 798 3762)
Brandandcomms@meristemng.com (+234 01 280 9250)

Meristem Finance Limited
olasokomubo@meristemfinance.com (+234 803 324 7996)
matthewawotundun@meristemfinance.com (+234 802 390 6249)

Corporate websites:
www.meristemng.com **www.meristemwealth.com** **www.meristemregistrars.com**

Meristem Research can also be accessed on the following platforms:

Meristem Research Portal: research.meristemng.com
Bloomberg: MERI <GO>
Capital IQ: www.capitaliq.com
Reuters: www.thomsonreuters.com
ISI Emerging Markets: www.securities.com/ch.html?pc=NG
FactSet: www.factset.com