Economic and Financial Review

Volume 52 | Number 4 Article 1

12-1-2014

Keynote address at the Executive Seminar on exchange rate policy and economic management in Nigeria

Godwin I. Emefiele
Central Bank of Nigeria

Keynote Address

Godwin I. Emefiele (CON) *

Deputy Governors,
Departmental Directors,
Branch Controllers,
Distinguished Resource Persons,
Executive Staff of CBN,
Members of the Media,
Ladies and Gentlemen.

It is indeed my pleasure to be part of this year's Central Bank of Nigeria Executive Seminar, and most especially, to present the keynote address. As it were, today's Seminar is the first to be held since I assumed the headship of the Bank and I have been reliably informed that the event had to be shifted to Abuja to secure my presence at the occasion in recognition of my tight schedule. I, therefore, commend the organisers – the Research and Human Resources Departments of the Bank – for their thoughtfulness, not only for making it easier for me to personally grace the occasion but also, for providing the opportunity for participants to deliberate on key developments in the global and domestic economic environments that directly or indirectly touch on a core mandate of the Bank.

Permit me to also seize this opportunity to appreciate the Management and the Executives of the Bank for providing the requisite capacity and qualitative leadership necessary for steering the affairs of the CBN, especially in discharging our responsibilities with the high level of professionalism and commitment expected of an ideal central bank operating in a dynamic global environment and a challenging domestic economic condition. Indeed, the Seminar provides a dual platform for interaction and brainstorming among the CBN Executives, on one hand, and with resource persons and other stakeholders on the other, given their immense expertise and experience on the subject matter. In this respect, the Seminar affords the external stakeholders the opportunity to better understand the position and the thinking of the Bank on issues bothering on the strategies for pursing its core mandate.

The theme for this year's Seminar "Exchange Rate Policy and Economic Development: Is There Need for A Paradigm Shift?", as well as the complementing sub-themes, are not only

---

* Mr Godwin I. Emefiele (CON) is the Governor, Central Bank of Nigeria

appropriate at this moment in our economic history, but have been carefully chosen, given the recent developments in the foreign exchange market that have elicited serious concerns from policymakers and other stakeholders in the Nigerian economy. By and large, the theme of the seminar, which has a strong bearing with the major planks of my vision for the Bank on assumption of office - ensuring exchange rate stability; building external reserves position; and preserving the value of the naira - unequivocally underscores the importance of the choice of an appropriate exchange rate regime in the economic management, given its strong linkage to economic competitiveness, domestic industries performance and economic progress.

Distinguished audience, as we all know, exchange rate is the price of a country's currency expressed in terms of some other currencies. It determines the relative price of domestic and foreign goods, as well as the strength of a country's external sector participation in international trade. In addition, exchange rate policy describes the techniques for the management – generation, accretion and disbursement – of foreign exchange resources in order to reduce the destabilising effects of short-term capital flows (Rodrik, 2008).

In the light of the above, it is obvious that Economists have long realised that poorly managed exchange rates can be detrimental for economic growth. Thus, they posited that avoiding exchange rate misalignment is one of the viable ways to ensure economic growth, particularly in the emerging and developing economies. This assertion was borne out of the fact that overvaluation adversely affect the competitiveness of the domestic industries, and is often accompanied by the shortage of foreign currencies, balance of payment disequilibrium, boom and burst macroeconomic cycles, all of which are inimical to economic growth.

Therefore, it is imperative for policymakers to be circumspect of their foreign exchange management techniques given the fact that the valuation (over/under valuation) regime has implications for the competitiveness or otherwise of the economy. It is instructive to note that the experience of many of the Southeast Asian economies, including India and South Korea suggests that pragmatic exchange rate management strategies was one of the most important factors in their economic growth experience. As you are also aware, skillful exchange rate policy was central to the ascendance of China on the global economic stage given the fact that its economic take-off was largely induced by currency undervaluation, which boosted domestic industrial production and stimulated net export component. Specifically, the international competitiveness of Chinese domestic industries became evident, thereby spurring China's economic growth and industrial exports, the aftermath of which made it the world's second largest economy as at today.

Distinguished ladies and gentlemen, exchange rate planning and management in developing and emerging economies like Nigeria are often very sensitive and controversial. This is most especially due to the domestic adjustments/reforms required to engender an appropriate rate that would bolster economic growth. As such, more often than not, adjustments are perceived by the citizens as damaging to the economies and most times are vehemently opposed by domestic public opinion.

You will recall that exchange rate management in Nigeria has undergone series of transformation/reforms over the years, influenced largely by domestic and external economic conditions, most especially, by issues surrounding federation revenue (government fiscal operations) as well as developments around crude oil (prices and volume of export), which is the mainstay of the country's foreign exchange earnings.

Specifically, Nigeria embraced the fixed exchange rate regime with its different variants in the immediate post independent period through the early 1970s and up until the mid-1980s. During this period, exchange rate regime transited from the domestic currency pegged at parity with British pound, later to pegging against a basket of convertible currencies and further to import-weighted basket approach. The oil price - induced external shock of the early 1980s exposed the overvaluation of the domestic currency, which resulted in economic meltdown and precipitated structural rigidities, financial repression, inflationary pressure as well as external imbalance.

Therefore, following Nigeria's economic crisis of the mid-1980s, which endured to the late 1990s, occasioned by the collapse of oil prices in the international market, it dawned on policy makers to address the problems of exchange rate misalignment. Consequently, the country embarked on the flexible/floating exchange rate regimes in 1986 with the adoption of the International Monetary Fund's (IMF) Structural Adjustment Programme (SAP); the country has kept faith with many of its variants up till today. Nonetheless, the main focus of the flexible/floating regimes has remained basically; to safeguard the value of the domestic currency, minimise speculative activities by reducing the premium between the official and other segments of the market, ensure unfettered financial intermediation and conserve the country's external reserves.

Ladies and gentlemen, the chronicle of the past events and efforts are imperative for us to understand the arduous task of exchange rate management. This is necessary in order to situate the task in proper perspective, particularly for the Nigerian economy, which is primary commodity resource based and heavily dependent on imports. Needless to say, the events of the past ten months, particularly with regard to the unbridled surge in demand for foreign exchange, the sharp drop in crude oil prices, low reserve accretion coupled with the attendant adverse effects on the exchange rate of naira, underscores the need for the assessment of our strategy.

A cursory examination of the facts would perhaps present a more vivid picture of the current situation with a view to appreciating the magnitude of the task ahead. For instance, the price of Bonny Light, Nigeria's premium crude, which sold for about US$114.07 per barrel in June 2014 consistently declined by 57.0 per cent to US$58.37 per barrel by February 2015.

In the same vein, sustained pent-up demand exerted pressure on the foreign exchange market resulting in significant depreciation of the exchange rate from an average of ₦162.82/US$ in June 2014 to ₦194.09/US$ at end-February 2015 at the inter-bank window, and from ₦167.14/US$ to ₦211.81/US$ at the Bureau de Change (BDC) segment of the market over the same period.

Ladies and gentlemen, we are all witnesses to the timely efforts taken by the Bank to restore confidence in the foreign exchange market and improve the general financial conditions. The deliberate adjustment of the exchange rate band was initiated to insulate the foreign exchange market from demand pressure bothering on speculative activities and at the same time stem the imminent depletion of the foreign reserves.

Similarly, the increasing usage of the US dollar in domestic transactions, which was observed to have fuelled the demand for foreign exchange, has attracted the attention of the CBN. In this respect, the Bank has taken corrective measures to address the concern. In addition, the utilisation of export proceeds has been restricted to eligible transactions only so as to block leakages. However, the persistent divergence between the inter-bank market and the bureau-de-change rates, which still provides avenue for arbitrage opportunities, is being seriously looked into.

Distinguish audience, let me remind us that the depressed outlook for crude oil price developments arising from the significant supplies of the US shale oil and the entrant of new producers into the crude oil market, the attendant low demand for Nigeria's crude oil by some of her trading partners, including the US has serious implications not only for reserves accretion but also for the sustenance of our foreign exchange market. Given this scenario, it is pertinent for this gathering to come up with useful policy ideas that would inform the Bank's future policy initiatives.

Distinguished audience, the Bank places a high expectation on the outcome of this Seminar given the array of erudite resource persons assembled to lead the discourse. Having set the stage for robust engagements by the participants, it is my fervent believe that with the array of resource persons, the Seminar will throw-up pragmatic ideas on the way forward based on dispassionate, realistic and factual analysis that would assist the Bank in navigating a terrain characterised by complex institutions, inadequate data and above all, the unpredictable behaviour of the market players.

Notwithstanding, with the downside risks associated with foreign exchange management, the CBN will continue to re-strategise its policy framework in line with international best practices to mitigate the inherent risks, strengthen the financial system and ensure macroeconomic stability.

Ladies and gentlemen, it is in the light of this that the gathering should be obliged to reappraise the subsisting exchange rate policy with a view to ascertaining if there is a genuine need for a shift in paradigm. It is my sincere hope that at the close of the Seminar the Bank would have a lot of options to take along towards improving policy making for the benefit of the economy.

On this note, I wish to declare the Seminar open and wish all of you a very rewarding and fruitful deliberation.

Thank you for your attention.