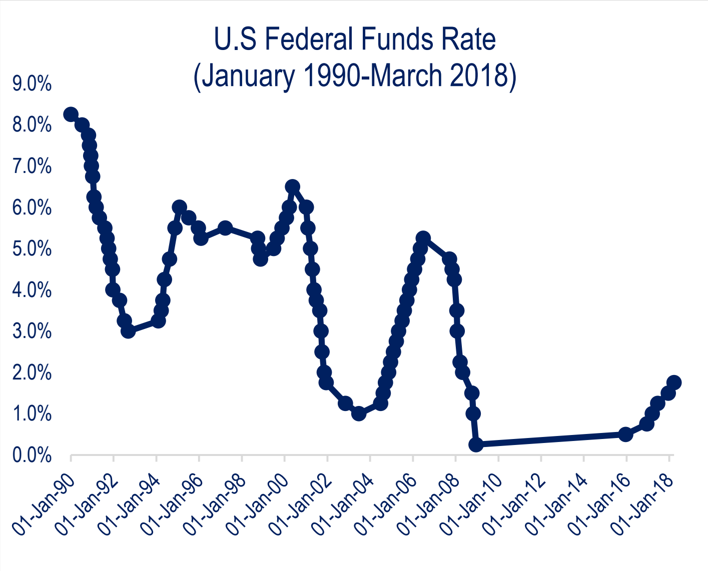
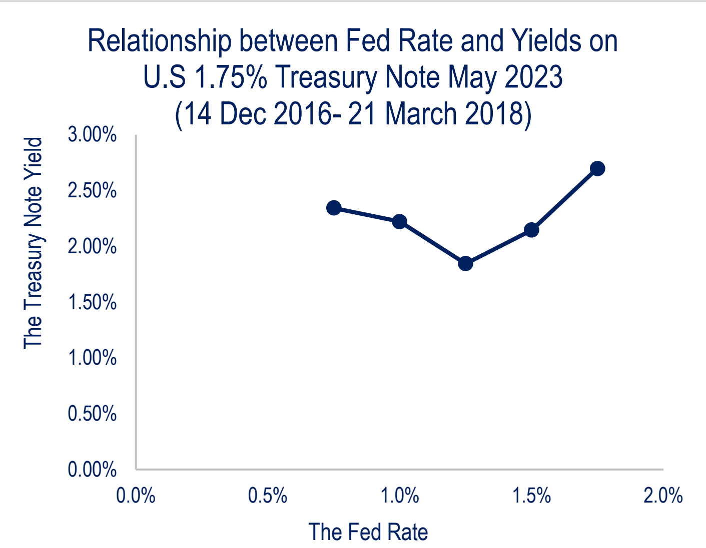
FOMC Raises Rate: Should Nigeria Lose Sleep?

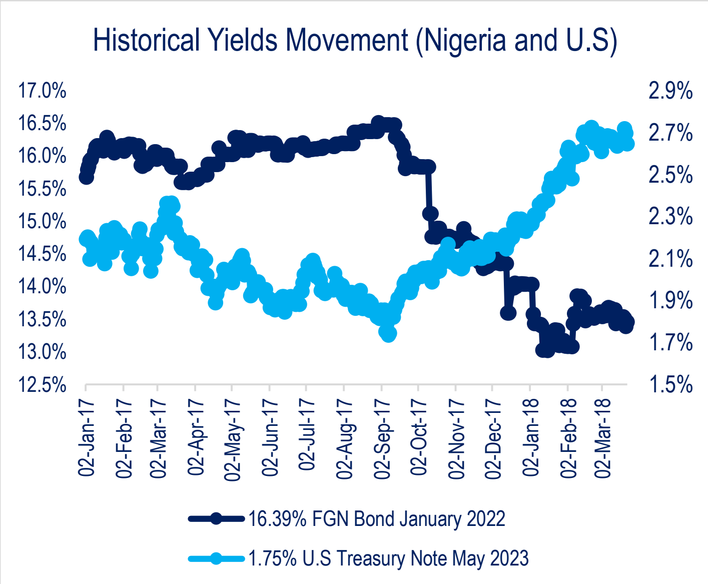
The Federal Open Market Committee (FOMC) of the U.S Federal Reserve System raised its anchor interest rate, the Federal Funds Rate (Fed Rate), to 1.50% - 1.75% from 1.25% - 1.50%. The FOMC announced the decision to raise the Fed Rate after its meeting on 21 March 2018. Given the impact of the increase in the Fed Rate on the global financial market, should Nigeria be concerned?



The hike in the interest rate is in line with the expectation of FSDH Research. We expect that the FOMC will increase the Fed Rate to 2.25% - 2.50% by year end. The FOMC notes the strengthening outlook of the U.S economy, the declining employment rate and the need to sustain inflation rate at 2% as the major reasons for the increase.

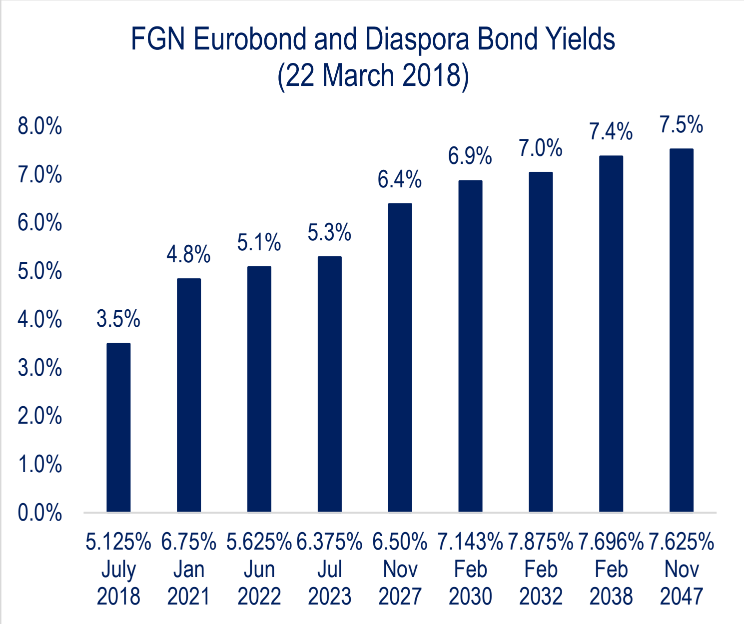


FSDH Research observes that between 14 June 2017 and 21 March 2018 the yield on the U.S 1.75% Treasury Note 2023 trended up as a result of hikes in the Fed Rate. We expect that a further increase in the Fed Rate will lead to additional increase in yield on the Treasury Note. The widening budget deficit in the U.S also supports increase in yields. Consequently, yields in the global market may increase.



The yields on the Nigerian Bonds maintained a downward trend since August 2017 following the strategy of the Debt Management Office (DMO) to increase external borrowing. The current yields on all the outstanding FGN's Eurobonds are lower than the coupon rates, reflecting the low interest rate environment in the international market.

The FGN announced a drop in borrowing through the FGN Bonds in March 2018. FSDH Research believes that the FGN will increase its borrowing through the FGN Bonds when the 2018 budget is signed into law, in order to cover its budget deficit. It may also increase borrowing from external sources in line with its debt management strategy. FSDH Research notes that the yields on the FGN Bonds may move up gradually from the current level before it drops around mid-year. In addition, subsequent external borrowing may attract higher interest rates as yields in the global market move up.



Sources: Debt Management Office; U.S Federal Reserve System, Bloomberg, and FMDQ

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