IMPACT OF MONETARY POLICY RATE ON PRICE STABILITY IN NIGERIA

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Abstract

Despite numerous monetary policy decisions by the CBN's Monetary Policy Committee, Nigeria's inflation rate (particularly in food, energy, and transport sectors) has remained persistently high. This study aims to assess the impact of the Monetary Policy Rate (MPR) on price stability in Nigeria. The paper is based on Central Bank of Nigeria (CBN) and National Bureau of Statistics (NBS) quarterly data generated for the period 2012 – 2025, which were analysed using the Dynamic Ordinary Least Squares (D-OLS) estimation technique. The results show that the MPR has a positive and significant impact on prices across these sectors, with a 1% rise in MPR leading to a 5.64% increase in food prices, 7.36% in energy prices, and 5.38% in transport prices. In contrast, the Lending Rate (LR) has a negative and significant impact on price across sectors, reducing food prices by 6.62%, energy prices by 6.23%, and transport prices by 5.19% for every 1% increase in the Lending Rate (LR). The study recommends that the Central Bank of Nigeria can use the MPR to manage inflation.

KEY WORDS: Dynamic Ordinary Least Squares (D-OLS), Inflation, Lending Rate (LR), Monetary Policy Rate (MPR), Nigeria, Price Stability.

JEL Code: C22, E31, E43, E52, O55**.**

1. Introduction:

Price stability is a cornerstone of monetary policy globally, as it is essential for promoting long-term economic growth and development. Ighoroje and Orife (2022) highlight that maintaining price stability has been a primary objective of monetary policy in both developed and developing economies. In Nigeria, the effectiveness of the Monetary Policy Rate (MPR) as a stabilisation tool is under scrutiny amidst persistently high inflation rates across various economic sectors. For instance, Nigeria's inflation rate surged to a record high of 33.88% in October 2024, up from

32.70% in September 2024, driven largely by rising transportation costs and food prices (NBS, 2024). In an attempt to control the rate of inflation in Nigeria, the Monetary Policy Committee (MPC) of the Central Bank of Nigeria has met thrice from January to May in the year 2024 alone. As argued by Sanusi (2012), price stability encompasses the stability of the currency's value (exchange rate), the cost of financial assets (interest rates), and the general price level (inflation). The European Central Bank (ECB) asserts that price stability, defined as the avoidance of prolonged inflation or deflation, is critical for high economic activity and low unemployment rates. Bernanke (2006) emphasises that price stability is both a goal of monetary policy and a means to achieve broader objectives, such as maximum employment and moderate long-term interest rates, while preserving the purchasing power of the currency.

The Monetary Policy Rate (MPR) is central to achieving price stability. It serves as the benchmark interest rate at which apex banks lend to Deposit Money Banks (DMBs) to regulate liquidity in the banking system. It anchors interbank money market rates and influences other economic variables, such as inflation and investment decisions (Bulus, 2010). The MPR is a vital tool for controlling short-term borrowing costs and targeting inflation rates to achieve price stability (Bilal et al., 2019).

Nigeria's economy is characterised by significant price instability due to heavy reliance on oil revenues and foreign economies. Persistent inflation, high unemployment, low output, and declining foreign reserves have exacerbated economic challenges. For instance, inflation increased from 18.8% in 2022 to 24.5% in 2023, with food prices surging by 35% and the naira depreciating by 95.6% following its floating in June 2023 (African Development Bank, 2024). These challenges prompted the Central Bank of Nigeria (CBN) to tighten monetary policy, raising the MPR from 17.5% in January 2023 to 18.75% in December 2023. Despite this, economic growth decelerated from 3.3% in 2022 to 2.9% in 2023, while poverty and income inequality remained high (African Development Bank, 2024).

This study therefore seeks to fill this gap by conducting a sectoral analysis of the impact of monetary policy rates on price stability in Nigeria from 2012 to 2025, with a specific focus on the agriculture, energy, and transportation sectors. By examining these critical sectors, this research

aims to provide a nuanced understanding of the relationship between MPR and price stability, offering valuable insights for policymakers and stakeholders.

2.1 Review of Related Literature

Several studies have explored the relationship between monetary policy and price stability both in the global and Nigerian contexts. Haruna et al. (2022) examined the effect of monetary policy on price stability in Nigeria using data spanning 1986 to 2020. Utilising ARDL and ECM models, their study revealed a long-term correlation between monetary policy variables and price stability. However, they highlight the persistent challenge of controlling inflation despite the Central Bank of Nigeria's continued efforts at adjusting the Monetary Policy Rate (MPR).

Akinjare et al. (2016) investigated the impact of monetary policy on Nigeria's economic development. The study adopted OLS to analyse time series data. The study found that interest rates, exchange rates, and money supply have a significant impact on economic development in Nigeria. Here, inflation was not shown to be a statistically significant variable. Imoisi et al. (2014) used annual data from 1970 to 2012 to examine the impact of monetary policy on macroeconomic variables like GDP, unemployment, inflation, and BOP. They used co-integration and the Error Correction Model. The study found a long-term correlation between monetary policy and selected macroeconomic indicators.

Ighoroje and Orife (2022) analysed the impact of exchange rate fluctuations on inflation in Nigeria from 1987 to 2019. Their analysis, based on OLS and GLS methods, used the nominal exchange rate as the primary variable alongside control variables like interest rates, money supply, imports, and GDP growth. They found that neither exchange rate fluctuations nor other macroeconomic variables significantly influenced inflation. Instead, they identified social and political factors, including unrest, consumer confidence, and the political environment, as key drivers of inflation.

Salisu (1993) analysed the relationship between interest rates and the demand for real cash balances using OLS and found no significant correlation. He concluded that using interest rates to influence money demand in Nigeria would likely be ineffective.

Omofa (1993) applied the Quantity Theory of Money (QTM) to assess the relationship between money supply and inflationary trends in Nigeria. While a positive correlation was observed, it was not statistically significant, suggesting that money supply is not the primary determinant of prices. Other factors, such as exchange rates and price-level lags, showed significant positive relationships with the current price level.

Nkoro (2005) examined monetary policy and macroeconomic instability in Nigeria from 1980 to 2000, highlighting factors such as financial sector instability, poor bank management, weak coordination between fiscal and monetary policies, and rising government expenditures as contributors to excess liquidity and inflationary pressures.

Using a rational expectations approach, Folawewo and Osinubi (2006) found that the Monetary Authority of Nigeria's efforts to control inflation and exchange rate volatility through reserves and credit policies had significant effects on the fluctuations of these variables.

Onayemi (2013) examined the impact of monetary policy on price stability and production growth in Nigeria from 1970 to 2011, using the Keynesian inflationary gap model. The results revealed that prior pricing gaps and changes in monetary aggregates significantly exacerbated inflationary pressures. Ineffective macroeconomic policies were identified as a key barrier to achieving price stability.

While monetary policy seeks to control the quantity and availability of money in the economy, as well as the conduit through which new money is supplied, the monetary policy rate is the interest rate at which the central bank lends to other banks, as well as the benchmark rate that determines the flow of credit to various sectors of the economy to stimulate investment and thus price stability. This study aims to evaluate the impact of the benchmark rate on price stability in major sectors of the economy: Agriculture, Energy and Transportation Sectors, which is the foundation for all other rates in the economy.

3.1 Model Specification

The model adopted is similar to those used by Bodunrin (2016), Abubakar (2012), Yakubu et al. (2013), Akinjaru et al. (2016), Ajisafe and Folorunso (2002), Adigwe et al. (2015), Ezinne (2020),

and Onehi et al. (2022). Unlike these studies, we made use of quarterly data that spans from 2010 to 2025. Furthermore, we made use of the sectoral Consumer Price Index (CPI) for the agriculture (FPI), energy (EPI), and transportation (TPI) sectors, which led to the development of three baseline models.

The baseline model is as stated thus:

$$CPI = f(MPR, LR, REER) \quad (1)$$

The disaggregated econometric model specification is given below, with the natural logarithm of the dependent variables taken:

$$lnFPI_t = a_0 + \beta_1 MPR_t + \beta_2 LR_t + \beta_3 REERt + \varepsilon_t \quad (2)$$

$$lnEPI_t = a_0 + \beta_1 MPR_t + \beta_2 LR_t + \beta_3 REER_t + \varepsilon_t \quad (3)$$

$$lnTPIt = a_0 + \beta_1 MPR_t + \beta_2 LR_t + \beta_3 REER_t + \varepsilon t \quad (4)$$

Where a_0 is the intercept/slope, β_1 to β_3 are the parameters; "t" denotes the study period in years involved, and the term ε_t is the error/disturbance term.

3.2 Justification for the Natural Logarithmic Transformation

The dependent variables are transformed into their natural logarithms to improve the estimation of the model. This transformation helps to stabilise the variance of the data, reduce the effect of extreme values, and make the relationship between the variables more linear. It also allows the estimated coefficients to be interpreted in percentage terms, making the results easier to understand and compare. Overall, the log transformation enhances the reliability and interpretability of the econometric analysis. The variable description, measurement and sources are discussed in Table 1.

Table 1: Study Variables, Symbol, Measurements, and Sources of Data

Variable	Symbols	Description and Measurement	Sources
Agricultural Price	FPI	This is captured by the Consumer Price Index (CPI) for Food and Non-Alcoholic Beverages, measured with a base index of November 2009 = 100	NBS (2024)
Energy Price	EPI	This is captured by the Consumer Price Index (CPI) for Housing, Water, Electricity, Gas, and Other Fuel, measured with a base index of November 2009 = 100.	
Transportation Price	TPI	This is captured by the Consumer Price Index (CPI) for Transport, measured with a base index of November 2009 = 100.	
Monetary Rate Policy	MPR	The benchmark interest rate the Central Bank of Nigeria uses to guide all other interest rates in the economy.	CBN (2023)
Lending Rate	LR	This is the interest rate charged by commercial banks to their most creditworthy customers for short-term loans.	
Real Effective Exchange Rate	REER	The Real Effective Exchange Rate (REER) is the value of a country's currency relative to a basket of major currencies, adjusted for inflation differentials, reflecting the country's trade competitiveness	

Source: Authors' construction, 2025

3.3 Estimation Technique

Dynamic Ordinary Least Squares (DOLS)

Dynamic Ordinary Least Squares (D-OLS), introduced by Stock and Watson in 1993, is an econometric method used to estimate long-run relationships among non-stationary time series variables that exhibit cointegration. D-OLS is particularly effective at addressing common issues

in cointegration models, such as endogeneity and serial correlation. The method adds leads and lags of differenced independent variables to the regression model, helping to eliminate bias from simultaneity between the error term and the regressors. This dynamic approach to OLS ensures that the estimators are both unbiased and consistent, even in the presence of non-stationary I(1) variables, making it a preferred technique for estimating long-run elasticities in macroeconomic studies. As a parametric method, D-OLS directly incorporates the dynamic structure of the system, capturing the short-run adjustments that lead to long-run equilibrium.

The dynamic ordinary least squares form of the model is given thus:

$$Y_t = \beta_0 + \beta_1 X_t + \sum P_i = 1\, a_i \Delta X_{t-1} + \sum q_j\, \beta_j \Delta X_{t+j} + u_t \qquad (5)$$

Where the dependent variable Y_t is a function of the independent variable X_t , its lagged and lead first differences, and an error term u_t. The coefficients α_i and β_j capture the impact of these lagged and lead differences on Y_t.

3.4 Trends of the Key Variables of the Study

Figure 1. Quarterly Composite CPI

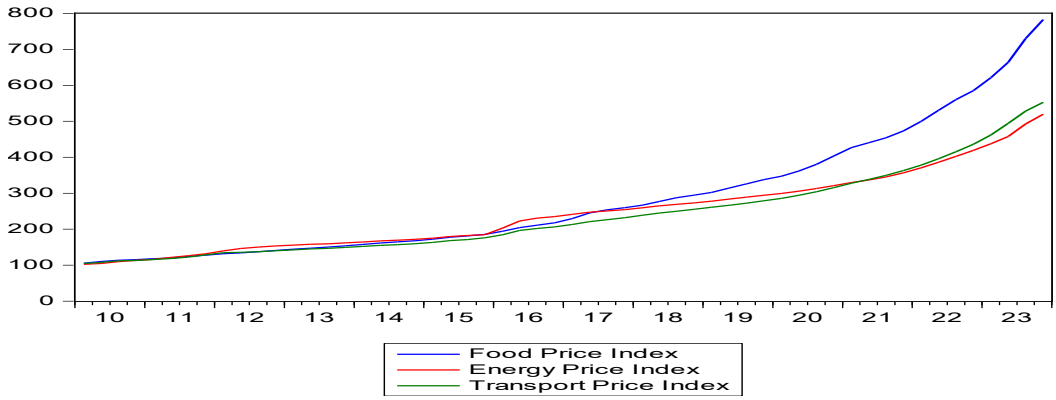

Figure 1 shows the quarterly trends of the Food Price Index, Energy Price Index, and Transport Price Index from 2010 to 2023. All three indices exhibit an overall upward trend, indicating rising costs over the period, with notable spikes in Q2 2016 and Q4 2020. These periods correspond to economic recession and the COVID-19 pandemic, respectively. The Food Price Index shows the

sharpest increase, particularly from 2020 onwards, reaching nearly an index of 800 in 2023, likely driven by supply chain disruptions and inflationary pressures. The Energy Price Index follows a similar upward trajectory but at a slower pace, reflecting fluctuations in energy costs. The Transport Price Index also rises steadily, influenced by increases in fuel prices and transport demand. These trends highlight the broader inflationary impact on essential goods and services, with food prices showing the highest sensitivity over the period

Figure 2. Interest Rates

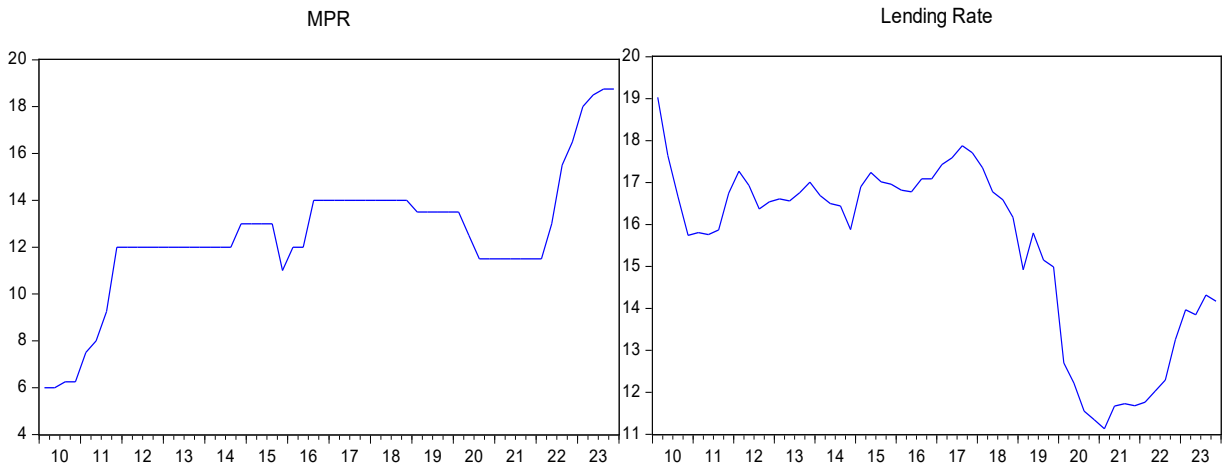

Figure 2 illustrates the trends in the Monetary Policy Rate (MPR) and lending rates from 2010 to 2023. The MPR shows a gradual increase from 6% in 2010, with significant adjustments around 2011 and 2016, reflecting monetary policy responses to economic conditions. Notably, sharp increases are observed in 2022 and 2023, with the rate peaking at approximately 18%. In contrast, the lending rate starts at about 19% in 2010 and gradually declines, with notable fluctuations around 2013 and 2017. A significant drop occurs between 2019 and 2021, reaching its lowest point near 11%, before recovering to approximately 14% by 2023. These trends highlight the interplay between monetary policy decisions and borrowing costs, with the MPR influencing lending rates over time in response to inflationary pressures and economic challenges.

4.1 Result Presentation and Discussion

The descriptive statistics provide insights into the characteristics of the study variables. Agricultural prices (LNFP), energy prices (LNEP), and transportation prices (LNTP) have similar

average values around 5.4, with moderate variations within their ranges. The monetary policy rate (MPR) averages 12.5%, with fluctuations between 6% and 18.75%, reflecting policy changes. Lending rates (LR) average 15.48%, with less dispersion, while the real effective exchange rate (REER) averages 80.42, indicating trade competitiveness fluctuations. These statistics reflect significant economic trends and variability in Nigeria.

Table 2. Descriptive Statistics

	LNFP	LNEP	LNTP	MPR	LR	'REER
Mean	5.488012	5.410755	5.368205	12.49554	15.47800	80.42214
Median	5.409916	5.472509	5.345948	12.00000	16.47000	78.03500
Maximum	6.663129	6.253154	6.315006	18.75000	19.03000	101.8100
Minimum	4.657256	4.626954	4.652494	6.000000	11.13000	59.07000
Observations	56	56	56	56	56	56

Source: Authors' computation, 2025

Correlation Results

The correlation matrix in Table 3 shows that the dependent variables of the study, namely the sectoral consumer price indices for food prices (LNFP), energy prices (LNEP), and transportation prices (LNTP), are highly positively correlated, with coefficients exceeding 0.98, indicating close movement.

Table 3. Correlation Matrix

	LNFP	LNEP	LNTP	MPR	LR	REER
LNFP	1.000					
LNEP	0.988	1.000				
LNTP	0.999	0.994	1.000			
MPR	0.712	0.772	0.739	1.000		
LR	-0.735	-0.675	-0.712	-0.196	1.000	
REER	-0.178	-0.165	-0.171	-0.090	0.420	1.000

Source: Authors' computation, 2025

4.2 Unit Root Test

Table 4 shows the results of the unit root tests carried out to determine the stationarity of the time series and their levels of integration. Employing the Augmented Dickey-Fuller and Phillips-Perron tests,

The results show that all the variables obtained stationarity after first difference. In this case, the most appropriate linear regression estimation is the dynamic DOLS test. But first, the Johansen cointegration test will be conducted to ascertain if there exists a long-run relationship between the variables.

Table 4. Augmented Dickey-Fuller and Phillips-Perron Unit Root Test Results

Variables	ADF		PP		Conclusion
	Statistics	Prob.	Statistics	Prob.	Integration
LnFPI	-5.005157	0.0008	-4.289986	0.0066	I (1)
lnEPI	-8.519633	0.0000	-3.541187	0.0105	I (1)
lnTPI	-3.179884	0.0267	-3.048374	0.0367	I (1)
MPR	-5.361634	0.0000	-5.419243	0.0000	I (1)
LR	-3.963080	0.0032	-5.985628	0.0000	I (1)
REER	-8.364935	0.0000	-8.273774	0.0000	I (1)

Source: Authors' Construction, 2025.

Cointegration Analysis

The Johansen Cointegration Test results in Table 5 reveal that there are four cointegrating equations at the 5% significance level, as indicated by the Trace test. In the Trace test, the test statistic exceeds the critical value for the hypotheses "None," "At most 1," "At most 2," and "At most 3," with p-values below 0.05, leading to the rejection of the null hypothesis of no

cointegration for up to four equations for Models 2, 3 and 4. This implies that at least four long-run relationships exist among the variables in the models, which supports the presence of cointegration among them.

Table 5: Johansen Cointegration Test

Unrestricted Cointegration Rank Test (Trace)				
Model 2				
Hypothesised		Trace	0.05	
No. of CE(s)	Eigenvalue	Statistic	Critical Value	Prob.**
None *	0.663025	147.3238	69.81889	0.0000
At most 1 *	0.580258	91.84867	47.85613	0.0000
At most 2 *	0.440585	47.57484	29.79707	0.0002
At most 3 *	0.263966	17.95083	15.49471	0.0209
At most 4	0.044479	2.320409	3.841466	0.1277
Model 3				
None *	0.545327	104.9705	69.81889	0.0000
At most 1 *	0.451259	64.77350	47.85613	0.0006
At most 2 *	0.397336	34.16692	29.79707	0.0147
At most 3	0.150828	8.340710	15.49471	0.4297
At most 4	5.03E-05	0.002563	3.841466	0.9572
Model 4				
None *	0.632937	121.8921	69.81889	0.0000
At most 1 *	0.479553	70.77872	47.85613	0.0001
At most 2 *	0.353351	37.47233	29.79707	0.0054
At most 3	0.193847	15.23881	15.49471	0.0546
At most 4 *	0.079942	4.249268	3.841466	0.0393
Trace test indicates 3 cointegrating eqn(s) at the 0.05 level				
* denotes rejection of the hypothesis at the 0.05 level				
**MacKinnon-Haug-Michelis (1999) p-values				

Source: Authors' Computation, 2025.

5.0 Discussion of Results

Impact of Monetary Policy Rate on Food, Energy, and Transport Prices

The results from Tables 4, 5, and 6 provide sufficient evidence of the significant influence of monetary policy variables on food, energy, and transport prices in Nigeria, revealing the interconnected nature of monetary policy and sector-specific price dynamics. The Monetary Policy Rate (MPR) consistently exhibits a positive and statistically significant impact across all three sectors, underscoring its role in shaping price levels. For food prices, as indicated in Table 4, a 1% increase in MPR leads to a 5.64% rise in food prices, reflecting how higher borrowing costs ripple through agricultural production and supply chains, raising costs for producers and consumers.

Table 6. Regression Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
MPR	0.056405	0.012445	4.532458	0.0001
LR	-0.066202	0.017804	-3.718369	0.0007
REER	0.006869	0.001598	4.299140	0.0001
C	4.410472	0.243146	18.13922	0.0000
R-squared	0.988867	Mean dependent var		5.496348
Adjusted R-squared	0.983919	S.D. dependent var		0.533939
S.E. of regression	0.067709	Sum squared resid		0.165041
Long-run variance	0.007380			

Source: Authors' Computation, 2025.

This finding aligns with the work of Haruna et al. (2022), who observed that monetary policy adjustments designed to control inflation might inadvertently elevate food prices by constraining the credit accessibility required for efficient agricultural production. Similarly, the energy sector, as shown in Table 5, experiences an even larger increase, with a 7.36% rise in prices following a 1% increase in MPR. This highlights the capital-intensive nature of energy production, where increased financing costs amplify operational expenses, a conclusion consistent with Chukwu's (2009) findings on the inflationary effects of monetary tightening on cost-sensitive sectors.

Table 7. Regression Result

Variable	Coefficient	Std. Error	t-Statistic	Prob.
MPR	0.073601	0.013844	5.316561	0.0000
LR	-0.062275	0.019806	-3.144308	0.0033
REER	0.006069	0.001777	3.414760	0.0016
C	4.456940	0.270482	16.47776	0.0000
R-squared	0.977895	Mean dependent var		5.423966
Adjusted R-squared	0.968070	S.D. dependent var		0.404600
S.E. of regression	0.072298	Sum squared resid		0.188171
Long-run variance	0.009133			

Source: Authors' Computation, 2025.

Transport prices, as presented in Table 6, follow a similar trend, with a 5.38% increase for every 1% rise in MPR, further emphasising the cascading effects of monetary policy on sectors reliant on both energy and infrastructure financing.

In contrast, the Lending Rate (LR) demonstrates a mitigating effect on prices across all sectors. For food prices, a 1% increase in LR reduces prices by 6.62%, suggesting that higher borrowing costs curb speculative trading and hoarding, thereby stabilising market supply. This finding aligns with the stabilising effects of real interest rates on consumer prices noted by Haruna et al. (2022). Similarly, in the energy sector, a 1% rise in LR corresponds to a 6.23% decrease in prices. Interestingly, this effect could stem from reduced demand for energy-intensive activities due to the higher cost of borrowing. Transport prices also experience a decline, with a 5.19% reduction per 1% increase in LR. This shows how elevated borrowing costs can suppress consumer spending and business activities, ultimately easing pressure on transport costs. These findings suggest that while the MPR serves as a broader inflationary force, the LR can act as a counterbalance, tempering price pressures in specific contexts.

The Real Effective Exchange Rate (REER) consistently exerts upward pressure on prices across all sectors. A 1% increase in REER leads to a 0.69% rise in food prices, reflecting the sensitivity of agricultural imports and inputs to exchange rate fluctuations. Similarly, energy prices increase by 0.61% for every 1% rise in REER, emphasising the importance of trade competitiveness and currency value in determining energy costs, particularly in an import-dependent economy like Nigeria. Transport prices also rise, although slightly less, by 0.57% for each 1% increase in REER, highlighting the indirect effects of currency dynamics on fuel costs and imported vehicles.

Table 8: Regression Results

Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
MPR	0.053798	0.011715	4.592337	0.0001
LR	-0.051911	0.016760	-3.097382	0.0038
REER	0.005676	0.001504	3.774151	0.0006
C	4.388614	0.228884	19.17396	0.0000
R-squared	0.986055	Mean dependent var		5.376891
Adjusted R-squared	0.979857	S.D. dependent var		0.429904
S.E. of regression	0.061014	Sum squared resid		0.134019
Long-run variance	0.006540			

Source: Authors' Computation, 2025

The robustness of these findings is seen by the high explanatory power of the models. R-squared values above 97% across all sectors indicate that the independent variables effectively capture the variability in prices. Adjusted R-squared values further affirm the reliability of the models after accounting for degrees of freedom, while the low standard error of regression and long-run variance estimates reflect precision and consistency.

5. Conclusion and Recommendations

In conclusion, the findings of this research highlight the significant and complex relationship between monetary policy and price levels in Nigeria, with a particular emphasis on food, energy, and transport prices. The results reveal that the Monetary Policy Rate (MPR) plays a central role

in driving price increases across these sectors, reflecting its broader inflationary effects, while the Lending Rate (LR) mitigates these pressures by reducing costs and stabilising prices. Additionally, the sensitivity of prices to fluctuations in the Real Effective Exchange Rate (REER) further underscores the multifaceted nature of price dynamics in Nigeria. These insights suggest that while the Central Bank of Nigeria (CBN) may use the MPR to control inflation, it is crucial to consider the unintended sectoral effects, particularly on essential sectors like food, energy, and transport. Therefore, it is recommended that the CBN adopt a more nuanced approach to monetary policy, ensuring that interest rate hikes are balanced with strategies to support sectors vulnerable to inflationary pressures.

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