



CENTRAL BANK OF LESOTHO

STATEMENT OF MONETARY POLICY COMMITTEE

21 September 2010

1. Introduction

At its 28th meeting held on 21st September 2010, the Monetary Policy Committee (MPC) of the Central Bank of Lesotho (CBL) discussed latest monetary policy operations, performance of the external sector as well as inflation-related developments to ensure that the price stability mandate of the Bank is being achieved. The Bank's objective is attained through the maintenance of an adequate level of Net International Reserves (NIR), which has been agreed as a minimum stock of USD956 million for the period July to September 2010 under the Extended Credit Facility (ECF) signed by the Government of Lesotho and the International Monetary Fund (IMF).

These reserves are kept to underwrite the fixed exchange rate between the South African (SA) rand and the loti, and to meet external obligations of the Government if in excess of foreign currency inflows. The currency peg allows Lesotho to benefit from the monetary policy actions of the South African Reserve Bank (SARB) as the bulk of inflationary pressures in Lesotho emanate from the South African market.

The MPC monitors performance of open market operations (auction of treasury bills) on meeting the NIR target.

2. Inflation Developments

The rate of inflation declined to 3.4 per cent on an annual basis in July 2010, from 3.8 per cent in the preceding month. The fall was influenced by a slowdown in non-food inflation, which registered 4.0 per cent in July 2010 against 4.4 per cent in June. Components of non-food inflation that decelerated included the transport component, which fell by 3.6 percentage points, as well as 'clothing and footwear', 'housing, water, electricity, gas and other fuels' and 'restaurants and hotels'. These dampened the effect of accelerating inflation in components such as 'furnishing, household equipment and routine maintenance for houses' and 'alcohol and tobacco'. The latter is the only component of inflation which recorded a double-digit annual inflation rate at 10.7 per cent in July 2010. Food inflation worsened to 3.4 per cent in July 2010 from 3.2 per cent the previous month.

Lesotho's inflation was the lowest in the Common Monetary Area (CMA) in the month under review. Annual inflation rate in South Africa was recorded at 3.7 per cent, within the 3 to 6 per cent range pursued by the South African Reserve Bank (SARB). This improved the outlook of inflation to 4.8 in 2011. This scenario promises low imported inflation in Lesotho in the next year.

3. Prospects on Maintenance of Price Stability

a. Balance of Payments

As envisaged by the Committee at its last meeting in August 2010, the current account deficit worsened to 23.8 per cent of GDP during the first quarter of the fiscal year 2010/11, which ended in June 2010. The deterioration was driven mainly by a significant fall in SACU non-duty receipts in the new fiscal year. The current account balance had registered a deficit equivalent to 7.0 per cent of GDP in the last quarter of the 2009/10 fiscal year. SACU non-duty receipts fell by more than 50 per cent in the quarter to June 2010, and coupled with a decline in income account, overshadowed a 1.7 per cent quarterly increase in exports and a decline in imports.

b. Fiscal Balance Outlook

Government budgetary operations deteriorated to a deficit of 26.0 per cent in the quarter to June 2010, from a deficit of 8.8 per cent in three months to March 2010. Total revenue fell by 17.8 per cent while expenditure and net lending rose by 6.4 per cent during the quarter. The decline in revenue mainly reflected a drop in SACU receipts, which weakened from a 60 per cent share of total government revenue in the first quarter of 2010 to 40.1 per cent in the second quarter, due to adverse effects of the global financial crisis on the customs revenue pool. The rise in expenditure was mainly influenced by payments of outstanding obligations from the previous fiscal year.

4. Monetary Policy Stance

Net International Reserves (NIR) were estimated at USD937.1 million on 17 September 2010, which was below the targeted minimum of USD956 million. The Committee resolved to undertake monetary policy action to improve the NIR level, which will be assisted by Government's efforts to contain expenditure.

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GOVERNOR

21 September 2010