



## CENTRAL BANK OF LESOTHO

### STATEMENT OF MONETARY POLICY COMMITTEE

18 December 2008

#### 1. Introduction

At its 17<sup>th</sup> meeting held on 18<sup>th</sup> December 2008, the Monetary Policy Committee (MPC) of the Central Bank of Lesotho (CBL) discussed the latest monetary policy operations, developments in the external sector and 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 foreign reserves. The reserves are kept to endorse the fixed exchange rate between the South African (SA) rand and the loti. This currency peg allows Lesotho to benefit from the monetary policy action of the South African Reserve Bank (SARB) as the bulk of inflationary pressures in Lesotho emanate from the SA market. Thus the MPC sets minimum target levels of external reserves and monitors performance of open market operations (auction of treasury bills) on meeting this target.

#### 2. Inflation Developments

The Committee noted that inflation rate peaked at 12.1 per cent in September and slowed down marginally to 12.0 per cent in October. The rise in food prices remained the main driver of inflation at 16.3 per cent. The non-food component of the Consumer Price Index (CPI) also experienced an increase during the period. It grew at an annual rate of 7.8 per cent, compared with a rise of 6.6 per cent at the time of the previous meeting of the MPC. However, the Committee noted the possibility of a

slowdown in overall inflation developments in the coming months. This is mainly due to a significant reduction in the price of international crude oil prices, which was trading at \$40 per barrel, compared to \$83 per barrel at the time of the previous MPC meeting. These developments were also translated into a cumulative decline in domestic petrol prices by more than R3.30 per litre since August.

The Committee observed that inflation in SA continues to be above the target of 3 to 6 per cent. However, there were signs of moderation in October because the measure of inflation targeted by the SARB, the CPIX, increased by 12.4 per cent after peaking at 13.6 per cent in August. Moreover, the SARB expects inflationary pressures to decline in the coming months as a result of the favourable international crude oil prices and a series of interest rate hikes effected since 2006. Indeed, household consumption expenditure and private sector credit declined in recent months. In addition, the SARB's MPC reduced its key interest rate in line with conditions prevailing in the global economy and in international financial markets.

### **3. Prospects for the Maintenance of Price Stability**

#### **a. Balance of Payments**

Net financial inflows in the balance of payments can increase domestic money supply and eventually exert upward pressure on prices. In the third quarter of 2008, the current account surplus was recorded at 9.3 per cent of GDP, following a 26.5 per cent of GDP in the second quarter. This was largely due to the higher volume of imports. However, official reserves continued to rise, registering 8.0 months of imports in the third quarter.

#### **b. Fiscal Balance Outlook**

The effect of a strong increase in external reserves on money supply continues to be moderated by decreases in net claims on government. Government budgetary operations resulted in an estimated surplus equivalent to 13.0 per cent of GDP in the third quarter of 2008. This was mainly aided by improvements in tax and non-tax

revenue. The non-expansionary fiscal policy helped contain domestically generated inflationary pressures.

#### **4. Monetary Policy Stance**

The Net International Reserve (NIR) position on the 12<sup>th</sup> December 2008 was US\$959.26 million. At this level, NIR is US\$459.26 million above the current NIR target and deemed sufficient to cater for trade with the rest of the world even in the presence of currency volatility. Thus the Committee decided to keep the NIR target unchanged at US\$450- 500 million.

M.P. Senaoana (PhD)

**GOVERNOR**

**18 December 2008**