CENTRAL BANK OF LESOTHO

STATEMENT OF MONETARY POLICY COMMITTEE

1 June 2010

1. Introduction

The Monetary Policy Committee (MPC) of the Central Bank of Lesotho (CBL) convened for its 26th meeting on 1 June 2010. The Committee deliberated on domestic monetary policy operations as well as developments in the world economy. The goal of MPC is to formulate and monitor the implementation of monetary policy in order to achieve price stability. Price stability is the overall objective of the Bank as stipulated by the Central Bank Act (2000).

2. Inflation Developments

The trend in the rate of inflation has remained flat at around 4 per cent in the first three months of 2010. This was driven by offsetting movements in the food and non-food components of the Consumer Price Index. The food index continued on a steady decline during the period, registering 3.0 per cent on annual basis in March 2010. This mainly reflected a slowdown in price increases of food items such as meat, bread and cereals. However, prices of fruits and vegetables continued to accelerate in the first quarter of 2010. The non-food component rose to 5.3 per cent in March 2010 from 4.8 per cent in December 2009. It was driven by acceleration in prices of miscellaneous goods and services, and education. The cost of education rose by 5.7 per cent in April 2010 compared with a 2.0 per cent increase in December 2010.

The trend of inflation in Lesotho remained consistent with price developments in the wider Common Monetary Area, which includes Namibia, South Africa and

Swaziland. The rate of inflation in South Africa fell from 6.3 per cent in December 2009 to 4.8 per cent in April 2010. South Africa expected its inflation to reach a low point of around 4.3 per cent in the third quarter of 2010 and to remain within the 3 to 6 per cent target band for the forecast period ending 2012. The low regional inflation could be attributed to the strong rand exchange rate, falling food inflation, relatively subdued oil prices and moderate aggregate demand.

3. Prospects for the Maintenance of Price Stability

a. Balance of Payments

The current account balance improved to a deficit equivalent to 9.1 per cent of GDP in the last quarter of the 2009/10 fiscal year, from a deficit of 14.4 per cent of GDP during the fourth quarter of 2009. The deficit was reduced by an improvement in diamond exports and current transfers. Thus, official reserves remained almost unchanged at 6.7 months of import cover.

b. Fiscal Balance Outlook

Government expenditure and net lending outstripped revenue by an amount equivalent to 8.8 per cent of GDP in the first quarter of 2010, following a surplus of 11.2 per cent of GDP in the preceding quarter. The deficit in the review period was driven by a surge in payments and settlement of government obligations as the fiscal year ended. A tight revenue outlook associated with lower economic activity and negative adjustments in customs revenue, coupled with an increase in government expenditure to boost fledging demand means that the Government may record a deficit during the fiscal year 2009/10, and beyond, after five years of surpluses. However, envisaged deficits are not expected to lead to unsustainable buildup in government debt. Government debt as a percentage of GDP stood at 40.3 per cent in March 2010, against a SADC macroeconomic convergence upper limit of 60 per cent. In addition, the Government is in negotiations with the International Monetary Fund for an Extended Credit Facility programme that would guide the economy to macroeconomic stability. Thus, the present government budgetary operations and its outlook are not expected to impact adversely on the inflation outlook.

4. Monetary Policy Stance

Net International Reserves (NIR) of the Central Bank of Lesotho were recorded at USD1.0 billion on 12 May 2010 following the latest monetary policy operations. At this level, the reserves were comfortably above the minimum level targeted by the Committee, which is USD700 million.

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