Central Bank of Lesotho

STATEMENT OF THE MONETARY POLICY COMMITTEE

February 1, 2022

1. The Central Bank of Lesotho (CBL) Monetary Policy Committee (MPC) held its 93rd meeting on February 1, 2022 to assess the adequacy of monetary policy targets. During the meeting, the Committee considered international, regional and domestic economic developments and financial markets conditions.

2. Global economy continues to remain under pressure from the prolonged effects of COVID-19. The International Monetary Fund (IMF) World Economic Outlook, released in January 2022, projected global growth at 4.4 per cent in 2022, a downward revision from 4.9 per cent estimated in October 2021. This was largely reflective of the continued emergence of new COVID-19 variants and on-going supply chain bottlenecks. Risks to the outlook were tilted to the downside and include new COVID-19 variants, supply chain disruptions, energy price volatility and rising debt levels.

3. Preliminary data indicated a strong growth in the United States (US) during the last quarter of 2021. Economic activity was supported by higher performance of manufacturing and services sectors, coupled with high personal consumption expenditure. On the contrary, the preliminary indicators pointed to slower growth in the Euro Area due to sluggish performance in manufacturing and services sectors. Growth in the UK was also expected to slow down during the fourth quarter of 2021, on account of resurgence of COVID-19 cases and a fall in consumer spending. In China, economic activity slowed to 4.0 per cent in the fourth quarter of 2021, compared to a growth of 4.9 per cent in the preceding quarter.

4. The global labour market conditions were expected to have worsened during the fourth quarter of 2021 on the back of subdued economic activity. In relation to price developments, inflation rose in many economies as a result of continued supply chain disruptions and rising energy prices. The monetary policy stance was tightened in some economies, as some central banks withdrew their stimulus on concerns of rising inflationary pressures.

5. Global financial markets indicators displayed elevated market risk amid fears around falling real wages. Yields in emerging markets, particularly in South Africa, remained largely unchanged with slight improvements on both the short and long ends of the curve. While foreign investors were net buyers of South African bonds and equity, the rand is expected to remain under pressure during the first quarter of 2022 due to the expected rate hikes in the US, policy uncertainty as well as energy supply challenges.

6. Domestic economic activity, as measured by the Monthly Indicator of Economic Activity (MIEA), was estimated to have improved by 12.2 per cent between October and November 2021, following five (5) consecutive months of negative growth. This was mainly due to improvements in both demand and production sides of the economy. The domestic economic growth is estimated to average 3.3 per cent over the medium term. Going forward, the major drivers of economic activity will be construction and the services industry.

7. While the domestic labour market conditions displayed mixed signals during the third quarter of 2021, the majority of the sectors recorded job losses. This was largely due to low external demand coupled with supply side disruptions. The domestic inflation rate, as measured by the year-on-year percentage change in the consumer price index (CPI), closed the year at 6.8 per cent. Contrary to the previous inflationary phases that were driven by food prices, the current phase is driven by energy and transport costs, with food prices somehow moderating the acceleration. The inflation rate is expected to average 5.2 percent over the medium-term. However, the possible adverse effect of recent heavy rains on food production and elevated prices of petroleum products present upward pressure to the inflation outlook.

8. The broad measure of money supply (M2) rose by 9.1 per cent during the fourth quarter of 2021 relative to a moderate growth of 0.3 per cent during the previous quarter. This was due to an increase in both the net foreign assets (NFA) and net domestic assets (NDA) during the review period. Credit to the private sector grew during the last quarter of 2021, albeit at a slower pace compared to the preceding quarter. Credit extended to the households grew by 3.2 per cent as a result of an increase in both personal loans and mortgages. This was, however, moderated by a 5.4 per cent decline in loans extended to business enterprises.

9. During the third quarter of 2021, the current account registered a deficit equivalent to 7.4 per cent of GDP, following a larger deficit of 10.2 per cent of GDP observed in the second quarter. This was driven mainly by improvements in the goods account driven by increased exports of diamonds, clothing and textiles, water and some agricultural products. However, poor performance of the services account, as well as the income accounts, dampened this improvement.

10. The Government budgetary operations recorded a surplus equivalent to 5.0 per cent of GDP during the last quarter of 2021 compared to a deficit of 11.7 per cent of GDP in the previous quarter. The stock of public debt was estimated at 57.2 per cent of GDP, compared to 59.5 per cent of GDP in the previous quarter.

11. In summary, notwithstanding the progress most countries made in vaccinations and policy support, the global economy enters 2022 in a weaker position than previously expected with risks to the outlook tilted to the downside. In particular, the global growth was vulnerable to new COVID-19 variants, supply chain disruptions, volatility of energy prices and rising debt levels. The outlook for the domestic economic growth has been revised downwards by an average of 0.2 percentage points in the medium term. Risks to the domestic economic outlook included an unpredictable path of COVID-19 pandemic and uncertain fiscal outlook.

12. Having considered the Net International Reserve (NIR) developments and outlook, regional inflation and interest rate outlook, domestic economic conditions and the global economic outlook, the MPC decided to:

i. Revise upwards the current NIR target floor of US$760 million to US$790 million. At this level, the NIR target will remain consistent with the maintenance of the exchange rate peg between the loti and the South African rand.

ii. Increase the CBL rate from 3.75 per cent per annum to 4.00 per cent per annum. The rate, set at this level, will ensure that the domestic cost of funds remains aligned with the rest of the region.

13. The Committee will continue to monitor the global developments and their likely impact on domestic macroeconomic conditions, especially the net international reserves (NIR), to take corrective action when needed.

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