June 18, 2013

Monetary Policy Committee Decision

Introduction

The June 18, 2013 meeting of the Monetary Policy Committee (MPC) concluded that the medium-term outlook continues to be positive, with the short-term forecast inflation remaining close to the upper end of the 3 – 6 percent objective range.

Economic Outlook and Assessment of Risks

Global output is projected to expand by 3.3 percent in 2013, up from an estimate of 3.2 percent in 2012. Economic performance in emerging market economies continues to be stronger than in advanced economies, but it is growing at a slower rate. The lower global growth, subdued demand and stable commodity prices have contributed to moderate inflationary pressures. Furthermore, persistent capacity underutilisation and high unemployment rates in major economies continue to restrain global inflation.

Domestic output increased by 3.7 percent in the twelve months to December 2012, with growth in the non-mining sectors slowing from 7.8 percent in 2011 to 5.8 percent in 2012, and the mining sector contracting by 8.1 percent. It is expected that output expansion will remain below potential in the medium term and will not be inflationary. Furthermore, it is anticipated that the impact of demand on economic activity will be modest, partly reflecting trends in government expenditure and personal incomes.

Inflation eased from 7.2 percent in April 2013 to 6.1 percent in May 2013, mainly due to base effects related to the May 2012 increase in administered prices, when inflation was 7.7 percent. Weak domestic demand and the forecast benign external inflationary pressures contribute to the positive inflation outlook in the medium term. In the short term, inflation is expected to be close to the upper end of the Bank's objective range of 3 – 6 percent. However, the projected underlying trend suggests a downward trajectory in inflation, thus enabling convergence to the medium-term objective range in the second half of 2013. This outcome could be adversely affected by any unanticipated large increase in administered prices and government levies, as well as international food and oil prices increasing beyond current forecasts.

Monetary Policy Stance

The current state of the economy, which is characterised by output growing below potential and high unemployment, provides an opportunity for non-inflationary stimulus to the economy. Assumptions on both the domestic and external economic outlook, as well as the inflation forecast, suggest that a more accommodative monetary policy stance is consistent with the achievement of the Bank's 3 – 6 percent inflation objective in the medium term. Accordingly, the Monetary Policy Committee decided to reduce the Bank Rate by half a percentage point to 8.5 percent.

Commercial banks are expected to make the necessary interest rate adjustments to reflect this policy decision.