PRESS RELEASE

BANK OF BOTSWANA'S FORMULATION AND IMPLEMENTATION OF MONETARY POLICY

The Bank generally values commentary and relevant critique of its operations and performance. However, when there are inaccuracies and misleading information, as has been the case in the recent past, it is important that they are addressed in order to ensure misrepresentations are corrected and important aspects of policy formulation and implementation are not distorted.

The policy framework that guides the work of the Bank's Monetary Policy Committee (MPC) is set out in the annual Monetary Policy Statement (MPS). This is in line with the statutory mandate of the Bank which prioritises the objective of price stability. In pursuit of this mandate, the Bank has set the objective, not a target, for inflation in the medium term of 3 – 6 percent to represent price stability in the Botswana context. Indeed stability of the monetary policy framework, based on the 3 – 6 percent medium-term objective range is now firmly entrenched. The inflation objective range is supported by the forecasting model as an attainable outcome. Therefore, the objective is appropriate in guiding inflation expectations in Botswana.

The Bank of Botswana implements monetary policy to achieve the inflation objective through a well-tested and conventional set of tools. These are the policy rate to signal changes in the direction of policy, open market operations, primary reserve requirements and moral suasion.

The transmission of monetary policy varies from country to country. However, it is generally acknowledged that interest rates play an important role in influencing domestic demand. There is no reason to believe that this is not the case in Botswana, as changes in interest rates either reduce or increase money that is available for alternative spending and, at the same time, affect the incentive to save or borrow. Moreover, the impact of interest rates strengthens as households are increasingly brought into the formal banking sector.

Inflation that is in the range of 3 – 6 percent approximates the average inflation for Botswana's major trading partner countries. This level of inflation creates a conducive environment for mobilising savings and investment, and fosters industry competitiveness, both of which contribute to sustainable economic growth, employment creation and higher living standards. Moreover, price stability helps to preserve the purchasing power and value of assets, especially for poorer households, thus contributing to the maintenance of decent living standards and less income inequality. Conversely, high inflation implies that price competitiveness of the domestic industry in foreign markets and against imported goods and services can only be achieved by continuous depreciation of the Pula exchange rate.

The Bank recognises that a wide range of factors, both internal and external, contribute to inflationary pressures. In particular, it is acknowledged that trends in international prices have a major impact on domestic inflation. Equally, changes in administered prices and indirect taxes have a significant bearing on inflation. The effect of these factors on past and prospective inflation is outlined in the 2013 MPS. The MPS itself points out that "the Bank will adjust monetary policy in response to a sustained deviation of the inflation forecast from the objective range, and where the causal factors could be influenced by domestic monetary policy action". In this respect, price movements that have tended to push inflation above the 3 – 6 percent medium term objective range in recent years mainly reflect factors and/or international price movements that cannot be influenced by monetary policy action.

It should be noted that the high proportion of imports in goods and services consumed in Botswana is not the principal reason why inflation is higher than the upper end of the inflation objective (6 percent). In recent years, domestic inflation has been persistently above inflation prevailing in trading partner countries, which is a clear indication that foreign factors were not the primary source of higher inflation. Even when finished goods are imported, a range of domestically determined costs (wages, utility tariffs, rentals, taxes, levies, etc.), as well as domestic demand conditions and competition will have a significant impact on the final price.

As a matter of routine, the Bank undertakes a comprehensive review of domestic and global economic developments, as well as the outlook for economic performance and inflation through, in the main, meetings of the MPC. This affords the MPC, which comprises relevant senior staff of the Bank, the opportunity to make timely determination of the monetary policy stance. The outcome of deliberations is published following every MPC meeting, and this attests to the Bank's transparency and accountability. The Bank also conducts economic briefings where, among others, the monetary policy framework and stance are outlined and clarified. Furthermore, the Bank's publications of interest to stakeholders, including members of the public, are available on the Bank's website (www.bob.bw). They include the Annual Report, Monetary Policy Statement and Botswana Financial Statistics.

It is significant that informed evaluation, surveillance and monitoring by the International Monetary Fund, through the annual Article IV surveillance missions, and the sovereign credit rating agencies (Standard & Poor's and Moody's Investors Service) annual reviews, have consistently endorsed and supported the Bank's monetary policy and its implementation.