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Statement of the Monetary Policy Management Committee (MMC)

1. Introduction

Following a thorough review of and intensive deliberations about the recent domestic and international economic developments, the Monetary Management Committee of the Bank of Namibia at its meeting of 7 June 2006 decided to increase the Bank rate by 50 basis points from 7.00 percent to 7.5 percent with immediate effect.

2. Developments in the real sector

Available economic indicators showed mixed performances in the activities of the real sector of the economy. A recovery was observed in some sectors of the domestic economy, while other sectors performed poorly. Stronger performance was exhibited in the production of diamond and zinc as well as in one indicator of consumer spending, namely motor vehicle sales. A decline was, however, registered, in the number of livestock marketed due to good grazing which enable farmers to rebuild their stocks.

3. Developments in inflation

The annual inflation rate continued to rise as observed since January 2006. The highest inflation rate of 4.6 percent was reached in March 2006, although it subsided slightly to 4.4 percent in April 2006. The average inflation for the first four months reached a level of 4.1 percent – higher than 2.1 percent registered at the same time in 2005 and 3.2 percent during the last four months of 2005.

The food and housing, electricity, fuel and gas categories were the main reasons behind the increase in the inflation. The food inflation averaged at 4.9 percent during the first four months of 2006 compared to 3.8 percent during the preceding period. The rain was reported to have been more than normal during the past rainy season and this has negatively affected the cereal harvest. The annual inflation for housing, fuel and gas also increased to 3.2 percent from 2.3 percent during the preceding period.

According to Bank of Namibia forecasts, the projected inflation for the year ending 2006 will average around 4.8 percent. The most important upside risks for inflation is the increase in international crude oil prices, the recent exchange rate depreciation and the increase in food prices. The oil prices have leapt above US\$72 a barrel settling at a record high. Although recently the rand exchange rate has come under pressure reaching N\$6.60 to the US dollar, it came as no surprise as it falls within the projected range. Therefore, the stability of the currency will continue to play a significant role in mitigating the effect of oil prices on the general price level. Also, if food prices continue to increase it may create further upward pressure on the overall inflation. Taking both the up and downside risks into consideration, the inflation is expected to remain within the range of 4.4 percent and 5.7 percent through to the first quarter of 2008 according to the Bank of Namibia's inflation forecasting model.

4. Exchange Rates

The external value of the Namibia Dollar (NAD) continued to be strong during the first quarter of 2006 although a depreciating trend was seen toward the end of April 2006. The depreciation of the Namibian dollar was reported to have continued during May 2006 to reach 11.80, 8.07 and 6.31 against the pound, Euro and the US Dollar, respectively.

5. Money Supply

On a quarter-on-quarter basis, the money supply showed a significant growth of 10.6 percent during the first quarter of 2006 in comparison to a slight increase of 1.8

percent noted during the same quarter of 2005. On the year-on-year basis, M2 grew remarkably by 16.5 percent during the first quarter of 2006. This rate is also higher than 11.3 percent recorded during the corresponding period of 2005. The growth in the M2 emanated mainly from the increase in the domestic credit extension.

6. Credit extension by Commercial Banks to private sector

The credit extension to the private sector continued to be strong, although growing at a slower rate. A year-on-year increase of 18.5 percent was observed during the first quarter of 2006, which is lower than 20.1 percent registered at the same time in 2005. Also, on the quarter-on-quarter basis, the growth in the private sector credit amounted to by 3.4 percent although weaker than 5.1 percent experienced during the fourth quarter of 2005. The lower increase in this quarterly development is attributed to the slowdown in credit extended to the other non-financial corporations.

7. Monetary Policy Stance

A recovery in the global economy was observed although the oil prices continued to be a threat to the inflation outlook. At home, there were improvements in the output of diamonds, zinc and gold, as well as in vehicle sales. Money supply and credit extension continued to be strong although slightly lower than in the comparable periods. Further, depreciation of the currency against the major international currencies was observed as from April onward.

Given the heightened concern about the risks of mounting inflationary pressures, the Bank of Namibia has decided to increase the Bank rate by 50 basis points from 7.00 percent to 7.5 percent with immediate effect. The Bank will continue to monitor the situation of sustained increases in international oil prices and its impact on the overall inflation and will take the necessary actions to maintain price stability.

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Governor