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PRESS STATEMENT

Monetary Policy Statement by the Bank of Namibia

1. Introduction

Since the last Monetary Policy meeting in June this year, the outlook on inflation has noticeably deteriorated. The less favourable outlook was primarily reflected in sharp increases in food and transport inflation. However, even if food and transport inflation are omitted from the consumer price index, the underlying inflation also shows a significant upward trend, raising concerns of second round effects of food and transport inflation. At the same time, there are encouraging signs of a cooling down in domestic demand conditions, as reflected in the latest vehicle sales and credit figures.

2. Developments in the Real Sector

On the international front, it is noted that the global economy continued to expand at a healthy pace during the second quarter of 2007, despite tight monetary policy in most of the world economies. Economic activity in the US remained relatively strong, with consumption growth supported by employment gains in the services sector. Activity in the Euro-zone and Japan continues to be strongly supported by robust domestic demand, while developing and emerging market economies continue to show solid growth rates on the back of the ongoing strong performance of China and India. Equally, the performance of the South African economy continued to be robust, with real GDP growth expanding by 4.7 percent in the first quarter of 2007. Overall in Africa, the short-term economic outlook remains positive against the backdrop of strong global growth, and the region's GDP growth is expected to accelerate to 6.9 percent in 2007 from 5.5 percent in 2006, according to the latest IMF projections.

In line with trends in the global arena, preliminary estimates indicate that economic activities in Namibia continued to show favourable performances, similar to what was reported previously. Most of the sub-sectors gained stronger growth momentum compared to the previous quarter. The mining and quarrying; electricity and water; hotels and restaurants; transport and communication and financial intermediation sectors, in particular, performed exceptionally well during the first quarter of 2007. Some other sectors such as agriculture, hunting and forestry and construction also displayed robust growth, albeit at lower rates than in the preceding quarter. However, the wholesale and retail trade sector growth slowed more significantly and this could be attributed to the tight monetary policy stance.

3. Credit Extension to the Private Sector

Credit extended to the non-government sector continued to grow at a declining rate. For instance, the annual growth rate in credit extension to the non-government sector slowed from 15.9 percent at the end of March 2007 to 13.4 percent at the end of June 2007.

The downward movement in the growth of credit extension was reflected in credit extended to both businesses and individuals. The annual growth in credit to businesses at the end of June was 10.1 percent, while that for individuals stood at 15.2 percent. The corresponding rates for March 2007 were 15.7 percent and 16.1 percent, respectively. It is also encouraging to note that the bulk of the increase in credit extension occurred in the mortgage category sub-sector, while the growth in instalment credit has decelerated. It is worth noting that growth in mortgage credit expanded at a healthy rate of 26.5 percent during June 2007, albeit slower than the 27.1 percent recorded in March 2007. In line with the decelerated growth in credit extension, there are also signs of slowdown in other demand indicators, such as the moderation in new vehicles sales, for which growth slowed to a monthly rate of 4.2 percent and an annual rate of 3.1 percent during July 2007. The comparative rates in June were 17.0 percent and 3.3 percent, respectively.

4. Inflation Developments

Since the last Monetary Policy meeting in June this year, the outlook on inflation has deteriorated further. Despite tighter domestic monetary conditions, inflation picked up to 7.2 percent in July from 7.0 percent in June 2007.

The factors that continue to contribute to the relatively high inflation rate are increases in food prices and transport inflation. However, even if the effect of higher food and transport prices are excluded, the underlying rate of inflation disturbingly persisted in July. This suggests that second round forces are at work, which is contributing to stronger inflationary pressures in Namibia.

In terms of food price inflation, there has been a downward trend in maize prices in June whilst wheat prices increased slightly. The decline in maize prices is, however, expected to be short-lived. Expected higher maize prices are also likely to influence meat prices significantly due to its impact on the price of fodder, although this impact might be somewhat offset by more livestock marketing because of the drought. This could, however, again be relatively short-lived as meat prices are expected to increase during the last quarter of 2007, due to the general increase in demand and the feedback effect from high food prices.

The persistent high and volatile international oil prices continues to be a worrying factor that drives inflation in a number of net oil importing countries, including Namibia. Due to supply uncertainties in major oil producing countries as well as the strong demand from the US, following a crude oil inventory decline, the international price of crude oil hovered around US$74 per barrel for the month of July 2007. As a result, the domestic fuel prices increased twice in a short period of time and further price increases cannot be excluded if the trend in international crude oil prices continues. Thus, more price pressure could come from this component going forward.

The South African Production Price Index (PPI), being a leading indicator for consumer price inflation in both South Africa and Namibia, showed a moderation of 10.4 percent during June 2007 compared with the 11.3 per cent during the preceding month. This decline is nevertheless expected to be short-lived. The PPI, and its concomitant impact on CPI, is expected to increase due to volatile oil prices and an expected increase in food prices, supported by increases in maize prices. Rising production prices are expected to filter through to consumer inflation in due course.

Having considered the latest inflation developments, forecasts and expectations, the Bank of Namibia considers the risks to the outlook for inflation in the medium term to remain tilted to the upside. Inflationary pressures are expected to persist, mainly on account of volatile crude oil prices and increases in administered prices effective from the 1st of August 2007. There is therefore a need for public utilities to exercise some restraint when considering increases in administered prices in order to contain further inflationary pressures.

5. Monetary Policy Stance

From the review of the recent economic developments, the Bank of Namibia noticed with concern the increase in the inflation rate since the last monetary policy meeting. At this stage, the growth in domestic demand seems to be abating as witnessed by the slowing growth in private sector credit extension and the number of vehicles sold. Nevertheless, rising food prices, the volatile exchange rate and international oil prices continue to pose major risks to the domestic inflation outlook. The Bank of Namibia is also concerned about the risks of second round effects of food and oil price inflation on the overall level of inflation. The risks to inflation, therefore, remain on the upside. The Bank of Namibia is, thus, of the opinion that an increase in the Bank rate is necessary to lessen the risks posed by these factors on inflation. In light of this, the Bank decided to increase the Bank rate by 50 basis points to 10 percent per annum, with effect from 17 August 2007. While tighter monetary conditions could moderate economic growth, the Bank believes that contained inflation is a more serious consideration at this stage than a situation of high economic growth with high inflation. Moreover, current economic performance is robust enough to be able to absorb tighter monetary conditions without significant negative impact.

As usual, the Bank of Namibia will continue to closely monitor price developments and factors that induce price changes, and will adjust its policy stance should monetary conditions so demand in the interest of price stability.

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