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Statement of the Monetary Policy Management Committee (MMC)

1. Introduction

The Monetary Management Committee (MMC) of the Bank of Namibia, at its meeting held on the 7th December 2006, reviewed the recent domestic and international economic developments. Based on these deliberations, the MMC decided to increase the Bank rate by **50** basis points from **8.50** percent to **9.00** percent with effect from Friday, 8th December 2006.

The Bank's monetary policy stance is based on the following considerations:

2. Developments in the Real Sector

Available indicators show that economic activities in Namibia picked up during the third quarter of 2006, contrary to the slowdown in most of the major economies, such as the USA, Euro-area, China and South Africa. The Japanese economy, on the other hand, continued to recover. The latest estimates in Namibia show that mining and quarrying performed exceptionally well, especially the diamond mining industry. In contrast, the agricultural sector continued to show poor performance due to a decline in livestock marketed amidst the prevailing favourable exchange rates and high meat prices. Despite the slightly more restrictive monetary policy pursued since August 2006, most economic activities show encouraging trends. We can, therefore, expect that the economy would reach a reasonable growth rate for 2006.

3. Inflationary Developments

The Namibian inflation continued to rise since the beginning of this year. It reached 5.8 percent in October from 5.5 percent in September 2006. The increase in the average annual inflation during October 2006 was mainly attributed to the rise in the inflation of food and transport. Other categories that exerted upward pressure on the inflation were alcoholic beverages and tobacco and miscellaneous goods and services, as a result of increased cost of financial services.

We do not expect the Namibian inflation rate to abate in the immediate future as further price increases are expected as reflected in the current rise of the South African Production Price Index (PPI). This rise is expected to create further inflationary pressures for Namibia given the fact that a sizeable portion of Namibian imports originates from South Africa. Responsible for the increase in the PPI come from both imported and South African produced goods. The PPI grew by 10.0 percent during October 2006 compared to 9.0 percent during the preceding month. The increase during October 2006 is quite significant when compared to an increase of only 4.2 percent recorded during the corresponding month of 2005.

4. Exchange Rates

Our analysis shows that the Namibia Dollar (NAD) depreciated steadily against the major currencies since the second quarter of 2006. The rapid depreciation of the Namibia Dollar since the first half of the year is, of course, an attractive bonus for the export industry, which is expected to improve its export earnings and therefore contribute to the increase in the foreign exchange reserves. The downside, however, is that it will exert inflationary pressure originating from imported goods. Responsible for the weakening of the Rand and consequently the Namibia Dollar, is the level of the current account deficit in the South African balance of payments, which, in turn, has resulted from the firm consumer demand in South Africa. The Namibia Dollar traded at a monthly average of N$7.65, N$14.34 and N$9.65 during October 2006 against the US Dollar, Pound Sterling and the EURO, respectively.

5. Money Supply

The significant rise in broad money supply (M2) on a year-on-year basis could be a concern, as it might be inflationary. The M2 rose considerably by 26.1 percent, as at the end of September 2006, compared to 7.9 percent recorded at the end of September 2005. The annual average growth in M2 for the first nine months of 2006 stood at 16.8 percent compared to 13.8 percent in the corresponding period of 2005.

6. Credit Extension by Other Depository Corporations to Private Sector

Although the growth in net domestic credit extended to the private sector slowed down recently, it is still considered too high and gives a good indication of the excess domestic demand in the economy. While the slowdown in growth could indicate the impact of tightened monetary policy, the transmission mechanism seems to be slow. The average annual growth in net domestic credit for the first nine months of 2006 stood at 17.8 percent compared to 20.4 percent during the corresponding period of 2005.

The slowdown in the growth of credit extension was a direct result of the decrease witnessed in credit extended to businesses, while the rise in that to individual households moderated that movement. The average annual growth in credit to businesses for the first nine months of 2006 was 13.7 percent, while that for individuals was 22.1 percent. The corresponding rates for 2005 were 8.9 percent for businesses and 25.7 percent for individuals.

7. Monetary Policy Stance

From the review of the recent economic developments, the MMC remained concerned about the unabated rise in inflation. Despite international oil prices slowing down, future developments are uncertain due to persistent threats of instability in some of the major oil producing countries. The robust domestic demand, money supply growth, high net domestic credit extension, generally high fuel prices, rising food prices and the depreciating domestic currency continued to pose a major risk to the domestic inflation outlook.

Considering the aforementioned economic developments, the MMC felt it necessary to take an appropriate monetary policy stance to lessen the risks posed by these factors on inflation. As a consequence, the MMC has decided to increase the Bank rate by 50 basis points from **8.50** percent to **9.00** percent. The MMC does not expect that the Bank rate adjustment will have a significant impact on the real economic activities, as it is mainly aimed at managing the consumer demand pressure resulting from the extension of credit. The Bank of Namibia will continue to do everything necessary to further tame future inflationary pressures in order to lessen its damaging impact on the Namibian economy.

Paul Hartmann

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