CENTRAL BANK OF
TRINIDAD & TOBAGO
POST OFFICE BOX 1250 PORT-OF-SPAIN, TRINIDAD, WEST INDIE
TELE: 625-4835, FAX: (868) 623-1955
E-Mail Address: info@central-bank.org.tt

MONETARY POLICY ANNOUNCEMENT

December 4th, 2015

Repo Rate Increases by 25 basis points

At its December 2015 meeting, Central Bank's Monetary Policy Committee (MPC) agreed to raise the "Repo" rate by 25 basis points to 4¾ percent. The MPC considered the impending start of U.S. monetary policy normalization to be the most influential factor behind its interest rate decision. The MPC also deliberated on the potential for rising inflationary pressures in early 2016 due to fiscal measures announced in the 2015/2016 Budget. Although this was the eighth consecutive hike in the Repo rate, the MPC still views the monetary policy stance to be accommodative enough to facilitate growth in the non-energy sector.

As 2015 draws to a close, the world economy remains fragile and vulnerable to setbacks. In October 2015, the International Monetary Fund downgraded its expectation for global growth from views expressed earlier in the year. However, the U.S. economy continues to strengthen, and with one Federal Open Market Committee meeting remaining for 2015, the Chair of the US Federal Reserve has left "open the possibility" for the Fed's first rate increase since June 2006 to occur in December 2015.

The Fed's interest rate lift-off could lead to bouts of market turbulence and reversals of capital flow in emerging economies, at a time when global financial markets are already volatile owing to uncertainty over China's growth prospects and falling commodity prices. The MPC continues to hold the view that higher domestic interest rates are necessary to enhance returns on TT$-denominated assets, helping to curb portfolio capital movements out of Trinidad and Tobago. Higher domestic interest rates are also necessary to discourage heavy consumer borrowing on imported consumer durables, which are a major source of foreign exchange demand.

The central banks in emerging markets such as Brazil, Colombia, Peru, Chile and South Africa have already begun to tighten monetary policy in order to address the possible threats stemming from the Fed's imminent move to increase interest rates.

Despite some volatility in food inflation, headline inflation has been relatively moderate to date, slowing to about 3½ percent in October 2015. After being subdued at about 2 percent over the first nine months of 2015, core inflation accelerated to nearly 2½ percent in October 2015, partly reflecting the 15 percent increase in the price of diesel and super gasoline announced in the 2015/2016 Budget.

The MPC considered the impact of VAT reform on inflation. If VAT is introduced at 12½ percent on all previously VAT-exempt items, most of which form part of the food basket, this could push core inflation to almost 3½ percent and food inflation into double digit territory. As a result, the MPC believes headline inflation could pick back up to around 5 percent in early 2016.

Trinidad and Tobago's economic growth prospects remain subdued amid weak business and consumer confidence. Following a dismal first half of 2015, domestic economic activity was depressed in the third quarter of 2015. The MPC was of the opinion that similar weak economic conditions are so far prevailing into the fourth quarter of 2015. Given the performance in the first nine months of the year and the potentially dimmed prospects for the final quarter, the domestic economy is expected to register an overall decline in 2015.

Since the last Monetary Policy Announcement in September 2015, there has been some fall-off in domestic liquidity levels to less than $3 billion. This was due to large one-off transactions such as payment of the proceeds from the Trinidad & Tobago Natural Gas Liquids (TTNGL) initial public offering to Government, and the record US$500 million foreign exchange intervention by Central Bank. However, with liquidity levels rebounding in late November 2015, the MPC decided to maintain its liquidity management programme so as to strengthen the impact of rising interest rates throughout the financial system. The median commercial bank prime lending rate increased from 8½ percent in September 2015, to 8¾ percent by November 23, 2015.

The next Monetary Policy Announcement is scheduled for January 29th, 2016.

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