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Monetary Policy Announcement

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ENERGY SECTOR REBOUNDS, CORE INFLATION STEADY: CENTRAL BANK MAINTAINS REPO RATE AT 2.75 PER CENT

As expected, the energy sector returned to positive growth in the fourth quarter of 2013, following the completion in September 2013 of significant, coordinated maintenance works by the two major natural gas producers and the downstream industry. The loss of oil output arising from the unanticipated December 2013 oil spills in Trinidad's south western peninsula did not adversely affect production activity in the energy sector in the fourth quarter. This rebound in the energy sector, coupled with the expected continued growth in the non-energy sector, suggests that the domestic economic recovery is continuing to gain traction. Core inflation was well contained towards the end of 2013. However, liquidity levels in the banking system remained elevated and by November 2013 business lending had contracted for an entire year. Meanwhile, the start to US monetary easing has prompted a narrowing of the interest rate differential between longer term TT and US treasury bonds, but evidence of disruptive portfolio outflows has not been observed. **In this context, the Central Bank views its accommodative monetary policy stance as still appropriate and has decided to maintain the 'Repo' rate at 2.75 per cent.**

Production in the energy sector improved in the fourth quarter of 2013. Natural gas output was more than 8 per cent higher than output in the third quarter of 2013, and had significant knock on effects to the downstream industry. Both methanol and ammonia production were higher by 20 per cent and 11 per cent (quarter-on-quarter), respectively. Notwithstanding the longer term environmental effects of the oil spills in the Gulf of Paria which are yet to be fully assessed, the loss of output did not significantly affect activity in the oil sector. Initial media reports suggest that roughly 7,500 barrels of oil were spilled, equivalent to less than 10 per cent of average daily oil production in the fourth quarter of 2013. Growth in the non-energy sector is expected to remain on trend in the fourth quarter of 2013.

Growth in private sector credit remained relatively steady in November 2013, supported by a noticeable uptick in consumer lending. On a year-on-year basis, private sector credit extended by the consolidated financial system rose by 3.4 per cent in November 2013, down slightly from 3.5 per cent in October 2013. In recent months there has been a notable expansion in consumer lending. On a year-on-year basis to November 2013, consumer loans grew by 7.5 per cent, the fastest growth rate recorded in more than two years. Growth in real estate mortgage loans also remained robust, expanding by nearly 14 per cent in November 2013. Business lending, however, contracted for the twelfth consecutive month, falling by just over 4.5 per cent in November 2013.

Liquidity levels in the banking system, while still relatively high, have fallen over the last few months. Commercial banks' excess reserves fell to a daily average of $6.4 billion over the period January 2 – 24, 2014, from a daily average of $7.1 billion in December 2013 and a record daily average of $8.4 billion in September 2013. During the first three weeks of January 2014, there was a small net domestic fiscal injection of approximately $75 million compared with an injection of $739 million in December 2013. The Bank rolled over a $1.5 billion special deposit that became due in December 2013. Central Bank's open market operations and sales of foreign exchange to authorized dealers helped to remove some of the excess liquidity from the financial system. Given the recently approved increase in the borrowing limits under the Treasury Bills and Treasury Notes Acts, the Central Bank will be intensifying its liquidity management operations in the coming months.

The domestic foreign exchange market has experienced some tightness since December 2013 due to higher seasonal demand and unexpected lower levels of foreign exchange conversions from the energy sector. Sales of foreign exchange to the public by authorized dealers amounted to about US$1,112.7 million in December 2013 - January 30, 2014, which outstripped purchases of US$823.6 million mainly from the energy sector. To support the market, the Central Bank sold US$40 million to authorized dealers in December 2013 and another US$160 million in January 2014.

According to the latest available data from the Central Statistical Office there was an up-tick in headline inflation in December 2013. On a year-on-year basis, headline inflation accelerated to 5.6 per cent in December 2013, from 4.4 per cent in November 2013 and a low of 2.7 per cent in October 2013. Core inflation remained unchanged at 2.0 per cent (year-on-year) in December 2013. For 2013, as a whole, core inflation was well contained, ranging between 1.9 – 3.1 per cent. Meanwhile, there was some increase in food prices towards the end of the year, with food inflation accelerating to 10.2 per cent compared with 7.3 per cent in November 2013 and 3.7 per cent in October 2013. In the coming months, if the oil-spills that occurred in the south-western peninsula worsen the longer term declining trend in the surrounding fish stocks, this may lead to some up-tick in fish prices and place upward pressure on food inflation.

The interest rate differential between the TT and US 3-month treasury rates remained near zero, measuring 1 basis point as at January 24, 2014. On the other hand, at the benchmark 10-year tenor, the interest rate differentials between TT and US treasury securities are in negative territory. However, with US treasury yields recently declining amidst a fresh wave of international concerns over emerging markets and indications of higher traded yields on TT securities, the differential between TT and US 10-year treasury yields narrowed to -12 basis points as at January 24, 2014 from -44 basis points in December 2013.

The Central Bank will continue to facilitate financial conditions supportive of the on-going recovery, while keeping evolving domestic and international economic and monetary conditions, including the impact of the US Federal Reserve's tapering programme, under close review in the coming months.

The next Monetary Policy Announcement is scheduled for March 28, 2014.

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