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Monetary Policy Announcement

November 29, 2013

ENERGY SECTOR CONTRACTS, CORE INFLATION SLOWS: CENTRAL BANK MAINTAINS REPO RATE AT 2.75 PER CENT

Planned large scale maintenance activity by the two major natural gas producers and coordinated maintenance shutdowns in the downstream industry in September severely contracted production throughout the energy sector in the third quarter of 2013. Partial information on non-energy sector activity, however, indicates a mixed performance in the third quarter of 2013, suggesting that the economy still remains on its path of slow but steady recovery. Core inflation has been well contained in the first ten months of 2013 and is expected to remain stable for the rest of the year. Food price inflation has also decelerated significantly to within single digit territory. However, liquidity levels in the banking system remain high and business lending contracted for the tenth consecutive month in September 2013. Meanwhile, despite a narrowing of the interest rate differential between longer term TT and US treasury bonds, there has been no evidence of disruptive portfolio outflows. **In this context, the Central Bank views the present accommodative monetary policy stance as appropriate and has decided to maintain the 'Repo' rate at 2.75 per cent.**

Large scale maintenance activity in the natural gas and downstream industries in September resulted in a sharp contraction of just over 4.0 per cent (year-on-year) in energy sector activity in the third quarter of 2013. The fall-off in natural gas production impacted the entire energy sector, with the production and exploration, and refining sub-industries contracting by 5.0 per cent and 2.3 per cent, respectively. With several companies aligning their plant turnarounds with the shortfall in natural gas production, there was also a contraction in petrochemical output. However, with the majority of the maintenance work completed, production in the energy sector is expected to return to more normal levels in 2014.

On a year-on-year basis, private sector credit granted by the consolidated financial system grew by 3.2 per cent in September 2013 compared with 2.9 per cent in August 2013. Consumer lending increased by almost 6.0 per cent in September 2013, slightly lower than the 6.3 per cent growth posted in the previous month but up from 2.3 per cent at the end of 2012. Commercial banks' consumer loans showed relatively strong growth for the purchase of motor vehicles (10.5 per cent), home renovations (7.1 per cent) and debt consolidation (17.3 per cent) in September 2013. Business lending, on the other hand, fell by 3.7 per cent in September 2013 compared with a decline of 5.8 per cent in August 2013 and growth of 1.0 per cent a year earlier. A sectoral examination of commercial banks' business loans showed contractions in lending to the finance, manufacturing and petroleum sectors. Meanwhile, real estate mortgage loans continued to grow at double digit pace.

Though there was some reduction in commercial banks' excess reserves from the highs experienced in September 2013, the financial system remained highly liquid in October and November 2013. After reaching a record daily average of $8.4 billion in September 2013, commercial banks' excess reserves at the Central Bank fell to $7.3 billion in October 2013. However, liquidity levels began to climb back up during the period November 1 – 22, 2013, with banks' excess reserves averaging $7.8 billion daily. Central Bank's open market operations and sales of foreign exchange to authorized dealers helped to absorb some of the excess liquidity. In the coming months, the Central Bank's liquidity management framework is expected to be enhanced by the recent approval to increase the borrowing limits under the Treasury Bills Act and Treasury Notes Act. This will facilitate the further use of open market operations to withdraw liquidity from the banking system.

In the face of high liquidity, short-term treasury rates remained relatively low, maintaining the narrow differential between the TT and US 3-month treasury rates in November 2013. In regards to longer term rates, the US treasury bond yields have risen recently. As such, the interest rate differentials between TT and US treasury securities at these longer term tenors are narrowing and in some cases are in negative territory. The TT/US 10-year treasury bond differential fell further to -29 basis points in November 2013 from -20 basis points in October 2013.

Latest available data from the Central Statistical Office showed that headline inflation continued to slow in October 2013. In the twelve months to October 2013, headline inflation decelerated to 2.7 per cent from 3.0 per cent in September and 5.1 per cent in August 2013. This was mainly due to a slowdown in core inflation which stood at 1.9 per cent in October 2013 from 2.9 per cent in the previous month. Meanwhile, after slowing to 3.0 per cent (year-on-year) in September 2013, food inflation rose to 3.7 per cent in October 2013. However, the recent heavy rains and resulting floods in Trinidad may lead to some up-tick in food inflation in the coming months.

The Central Bank will continue to facilitate financial conditions supportive of the recovery, while keeping domestic and international economic and monetary conditions under close review in the coming months.

The next Monetary Policy Announcement is scheduled for January 31, 2014.

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