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

MONETARY POLICY ANNOUNCEMENT

March 28, 2014

CAUTIOUS OPTIMISM FOR ECONOMIC OUTLOOK; CENTRAL BANK MAINTAINS REPO RATE AT 2.75 PER CENT; INTENSIFIES LIQUIDITY MANAGEMENT

Since January 2014, downside risks to global growth have receded somewhat, especially with improving economic prospects for both the United States and core euro area economies. Nevertheless, financial conditions have tightened further in some emerging market economies with external vulnerabilities. More recently, the escalation of tensions in Venezuela and between Russia and mainland Ukraine have added to geopolitical risks. The US Federal Reserve continued to reduce the pace of its monthly asset purchases programme, and gave guidance in March 2014 that policy interest rates could increase even faster than initially anticipated.

On the domestic front, results from the first Business Confidence Survey suggest that the business community is cautiously optimistic about the strength of the Trinidad and Tobago economy within the next 6-12 months. Business lending, however, contracted for the fourteenth consecutive month in January 2014, but at the slowest rate of decline in the past year. Although there was some acceleration in core inflation in February 2014, underlying inflationary pressures are still well contained. Inflationary pressures are likely to build up later in the year as economic activity ramps up. At the same time, liquidity levels in the banking system remain high and continue to keep domestic treasury rates low. With US treasury rates rising in recent months, interest rate differentials on longer term TT and US treasury bonds are negative. Therefore, the Central Bank will be intensifying its liquidity management operations in the coming period to reduce excess liquidity in the banking system.

In light of these circumstances, the Central Bank has decided to maintain the 'Repo' rate at 2.75 per cent while its liquidity absorption measures take effect. The Bank will continue to monitor developments in the market and is prepared to take further action as appropriate.

According to the Central Bank's Business Confidence Survey, done in conjunction with the Arthur Lok Jack Graduate School of Business, in the first quarter of 2014 the local business community was most confident that the financial performance of their businesses would improve within the next 6 to 12 months. In addition, firms were optimistic that their production levels would increase in the next 6 to 12 months. Executives were less confident (though still optimistic) that they would increase their capital investments and employ more workers in the short-term.

Growth in private sector credit picked up in January 2014. On a year-on-year basis, private sector credit granted by the consolidated financial system rose by almost 5.0 per cent in January 2014, up from around 3.5 per cent in December 2013. The expansion in private sector credit was driven by higher demand for consumer and real estate mortgage lending. Consumer loans revealed strong growth for bridging finance, home renovations and purchases of motor vehicles. Growth in real estate mortgage loans remained robust, expanding by 14.5 per cent in January 2014. Business lending by banks, however, continued to decline, albeit at the slowest rate (0.8 per cent) since December 2012.

Liquidity levels retreated in January 2014 before rising again in February to March 2014. After declining to $6.4 billion in January 2014, mainly because of lower Government fiscal injections, commercial banks' excess reserves at the Central Bank rose to a daily average of $6.7 billion in February 2014. Average excess liquidity rose again to $7.1 billion over the period March 5 – 24, 2014, as fiscal injections rebounded. Open market operations and Central Bank sales of foreign exchange to authorized dealers together withdrew $893 million in January, $831 million in February and $395 million in the first three weeks of March 2014. In addition, the Central Bank also rolled over for one year, a $1.5 billion commercial bank special deposit which matured in March 2014. Following the Gazetting of Parliament's approval of increased borrowing limits under the Treasury Bills and Treasury Notes Acts, the Central Bank is now in a better position to expand its open market operations to remove excess liquidity from the banking system.

The domestic foreign exchange market remained relatively tight in February and most of March 2014. Over the period February – March 24, 2014, purchases of foreign currency by authorized dealers from the public amounted to US$691 million, while sales amounted to US$872 million. The resulting gap of roughly US$181 million was met by Central Bank's sales of foreign currency to authorized dealers. On March 5, 2014, the Central Bank undertook a special intervention of US$50 million to meet immediate US dollar, trade-related demand of small and medium enterprises. Conversions are expected to increase towards the end of March 2014, as energy sector companies prepare to meet their quarterly tax obligations.

High liquidity levels kept domestic short-term treasury rates relatively low. The interest rate differential between the TT and US 3-month treasury rates stood at 1 basis point as at mid-March 2014. Longer term US treasury rates rose following the US Federal Reserve's announcement on March 19, 2014. As a result, the differential between TT and US 10-year treasury yields widened further to -12 basis points as at March 21, 2014, from -3 basis points at the end of February 2014.

According to the latest available data from the Central Statistical Office, in the twelve months to February 2014 headline inflation measured 3.9 per cent, which was up from 2.9 per cent in January 2014 but down from 5.6 per cent in December 2013. Core inflation accelerated to 2.7 per cent (year-on-year) in February 2014 from 2.0 per cent in December 2013. There was a pick-up in the 'entertainment' related sub-categories such as recreation and culture, hotels, cafes and restaurants and alcoholic beverages and tobacco in early 2014. On the other hand, food inflation decelerated to 5.2 per cent in February 2014 from 10.2 per cent in December 2013.

The next Monetary Policy Announcement is scheduled for May 29, 2014.