Economic Association of Namibia

PO Box 6148
Windhoek, Namibia
M +264 81 155 9775
F: +264 88 622 267
E: info@ean.org.na
W: www.ean.org.na

EAN Commentary

Date: 17 August 2017

BoN releases Monetary Policy Statement

The Bank of Namibia has released the Monetary Policy Statement on 16 August 2017. The Monetary Policy Committee has decided to cut the repo rate by 25 basis points from 7.00 percent to 6.75 percent. The BoN has followed the step taken by the South African Reserve Bank that cut the repo rate by 25 basis points to 6.75 percent with effect of 21 July 2017.

The Bank of Namibia cited the following main reasons for its decision:

- Slightly better global economic growth prospects for 2017 (3.5 percent) compared to 3.2 percent in 2016. However, global risks remain such as policy shifts in the USA and the UK (Brexit) and geopolitical tensions in particular between the USA and North Korea.
- Weakening domestic economy during the first six months of 2017 compared to the same period 2016. This affected mainly the construction, manufacturing, wholesale and retail trade, as well as the transport sectors.
- Although the domestic inflation rate for the first six months averaged at 7.00 percent compared to 6.3 percent during the same period in 2016, it is on a downward trend.
- Private sector credit extension (PSCE) slowed down significantly from 12.5 percent during the first six months in 2016 to 8.5 percent in 2017.
- Increased stock of international reserves that cover 5.5 months of imports and are sufficient to sustain the currency peg of the Namibia dollar with the South African rand.

EAN comments

The repo rate determines the interest rates of commercial banks. An interest rate cut has therefore positive impacts on the cost of borrowing, since commercial banks usually adjust their interest rates by the same margin.

- The foreign exchange reserves have seen a substantial recovery due to the African Development Bank loan issued in South African rand and the repatriation of funds by financial institutions. The import cover increased from about three months to 5.5 months, which is a very good news. The low import cover in the past had been of concern. However, the Eurobond and AfDB loan have to be repaid at some point in time.
- The strong recovery of foreign exchange reserves reduces the need for an attractive interest rate environment to attract foreign financial investment.
- Although the inflation rate exceeded last year's average inflation rate for the first six months, we expect the annual inflation rate for 2017 to be lower than in 2016. Even though the annual inflation rate is expected to stay outside the band of 3 to 6 percent, the downward trend supports the interest rate cut.

- The lower interest rate is good news for borrowers, since it reduces the costs of borrowing.
- The lower interest environment could support consumption, which would directly benefit the wholesale and retail trade sector and consequently the manufacturing sector.
- It could also encourage private sector investment, since lower interest rates reduce the cost of doing business and could make investment more viable. However, in order to support private sector investment, Namibia has to improve the policy environment.
- The decision is good news for the public sector, since it could cushion against potentially increasing costs of borrowing owing to the investment downgrading by Moody's on 11 August 2017.
- However, lower interest rates disincentivise savings since returns from savings decline. Combined with lower costs of borrowing could increase household indebtedness further, which is already at a high level.