

Statement of the Monetary Policy Committee

28 August 2019

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to lower the Bank's interest rates by 0.25 percentage points. The Bank's key interest rate – the rate on seven-day term deposits – will therefore be 3.5%.

According to the Bank's new macroeconomic forecast, published in the August *Monetary Bulletin*, this year's economic contraction will measure 0.2%, slightly less than was forecast in May. This is due mainly to more resilient private consumption growth, although the contribution of net foreign trade is also more positive, as demand has shifted towards domestic production, partially offsetting the stronger contraction in tourism. The GDP growth outlook for 2020 has deteriorated, however, as it now appears that it will take longer for tourism to recover after this year's setbacks.

Inflation measured 3.4% in Q2 but fell to 3.1% in July. Underlying inflation has developed in a broadly similar manner. Furthermore, inflation is expected to subside faster than was forecast in May and align with the target in H1/2020. The króna has appreciated by just over 2% between meetings, and the foreign exchange market appears well balanced. Inflation expectations have fallen back to target since the MPC's last meeting, and the monetary stance has therefore tightened slightly.

Near-term monetary policy decisions will depend on the interaction between developments in economic activity, on the one hand, and inflation and inflation expectations, on the other.