Statement of the Central Bank of Iceland Monetary Policy Committee

Central Bank interest rates lowered

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to lower the Bank's interest rates by 0.75 percentage points. The deposit rate (current account rate) will be 4.0%, and the maximum bid rate for 28-day certificates of deposit (CDs) will be 5.25%. The seven-day collateralised lending rate will be 5.5% and the overnight lending rate 7.0%.

Inflation continued to subside in September and October, after a marked decline since March of this year. The CPI rose 3.3% year-on-year in October, or 2.6% excluding consumption tax effects, which is close to the inflation target. Weak economic activity, declining inflation expectations, and this year's appreciation of the króna continue to support low and stable inflation.

According to the forecast published in *Monetary Bulletin* today, the economy will be somewhat weaker this year and in 2011 than the Central Bank had forecast in August. However, recovery is still expected to begin in the second half of this year. Inflation has subsided faster than was forecast in August, and the outlook is for inflation to be at target by year-end, fall below 2% next year, and subsequently return to target.

Since the MPC's September meeting, the króna has appreciated by nearly 1% in trade-weighted terms but has weakened slightly against the euro. As expected, the Central Bank's regular purchases of foreign currency, which commenced on 31 August, appear not to have had any marked effect on the króna. The capital controls, developments in terms of trade and other factors affecting the current account balance, and the monetary policy stance relative to trading partner countries all continue to support the exchange rate.

The Monetary Policy Committee considers that, if the króna remains stable or appreciates and inflation subsides as forecast, the premises for some further monetary easing should be in place. However, the prospect of removing the capital controls creates uncertainty about short-term room for manoeuvre. The MPC stands ready to adjust the monetary stance as required to achieve its interim objective of exchange rate stability and ensure that inflation is close to target over the medium term.