

Statement of the Monetary Policy Committee 19 May 2021

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to raise 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 1%.

The economic recovery in H2/2020 was stronger than previously assumed. According to the Central Bank's new macroeconomic forecast, published in the May issue of *Monetary Bulletin*, the outlook is for just over 3% GDP growth this year and more than 5% growth in 2022. The outlook has improved since the Bank's last forecast, owing largely to signs of a stronger recovery of domestic demand. Unemployment has eased, although it remains high. The slack in the economy therefore appears to be smaller and looks set to close sooner than previously estimated.

Supply-side disruptions due to the COVID-19 pandemic have pushed production and distribution costs upwards worldwide, and global oil and commodity prices have risen steeply in the recent term, although these increases may prove to be temporary.

Inflation has therefore been higher and more persistent than previously forecast, measuring 4.6% in April. Inflationary pressures appear to be widespread, as underlying inflation is broadly similar to headline inflation. This is due to a number of factors, including the depreciation of the króna in 2020 and steep rises in wages and house prices. As a result, it is necessary to raise the Bank's interest rates in order to ensure that inflation expectations are anchored to the target.

The MPC will apply the tools at its disposal to ensure that inflation eases back to the target within an acceptable time frame.