

CENTRAL BANK OF THE DOMINICAN REPUBLIC

Economic Note

The Central Bank of the Dominican Republic, in conformity with its policy of transparency and accountability, wishes to inform economic agents and the general public the rationale behind the decision to adjust interest rates for fixed term investment deposits placed through the direct facility.

This decision is consistent with the set of actions taken since early in the year, with the objective of diminishing the impact of internal and external factors influencing the price level in the economy. To control inflationary pressures, the Central Bank has striven to assure that the money in circulation and the marginal cost of available funds in the financial sector reflect the current stance of monetary policy.

The measures that the Central Bank has adopted have contributed to reduce the level of credit extended to the private sector. This, together with the fiscal adjustment package announced last July by the Executive Branch, should contribute to slow down aggregate demand and reduce pressure on the current account.

Regarding the balance of payment, sustained activity in the import sector, particularly in the trade for fuel, food, and other commodities, have influenced the net position of the economy and led to a deterioration of the current account deficit. At the same time, higher import prices have generated a multiplier effect on the cost of the main components of the basic market basket of goods and services. This effect on the demand for imported goods has occurred in spite of the weakening in the terms of trade.

Internally, the interest rate adjustment seeks to reduce the monetary base, which has increased in level and volatility since early July, reflecting greater liquidity in the economy. In the money targeting framework operated by the Central Bank, the monetary base serves as an operating variable and as a signal of the monetary policy stance.

This rate adjustment will contribute to achieving the Central Bank's demonetization efforts, which will help anchor inflation expectations and maintain the monetary base within the target range established in the Monetary Program for 2008. During this year, other central banks in the Latin America and the Caribbean region have been adopting similar measures, especially those who are non-oil producing and commodity importers countries.

The Central Bank will continue to monitor internal inflation risks as well as the international markets, with the objective of adopting timely remedies whenever necessary.