SECRETARIA DEL BANCO

The Central Bank reduces its Monetary Policy Rate by 50 basis points

At its July 2017 monetary policy meeting, the Central Bank of the Dominican Republic (BCRD) reduced its monetary policy interest rate by 50 basis points, from 5.75% to 5.25% per annum, effective as of 1 August. According to the short-term liquidity management scheme of the BCRD, the rate corridor was adjusted in the same ratio, indicating that interest rate of the short-term deposit standing facility (overnight) decreased from 4.25 to 3.75% per annum, and the rate of the expansion facilities (repos) is reduced from 7.25% to 6.75% per annum.

The decision on the reference rate took into account the risk balance of inflation projections, the evolution of the main domestic macroeconomic indicators, the relevant international environment and the market expectations. Year-to-date inflation in the first half of the year was 1.02%, while the year-on-year inflation in June fell to 2.55%, below the lower limit of the target range of 4% ± 1% established in the Monetary Program. Likewise, the year-on-year core inflation, related to the monetary conditions, was 2.18%. According to the most recent projections, inflation would approach the lower limit of the target range in the monetary policy horizon.

Since last year, three external factors have conditioned the behavior of the Dominican economy: (1) the reversal of the positive supply shock associated with international oil prices, that had benefited the Dominican economy in recent years; (2) the Federal Reserve of the United States of America (USA) resumed the normalization process of its monetary policy; and (3) higher uncertainty surrounding the new US government's economic policies.

However, since the last increase in the monetary policy rate in March, the international environment has changed. On one hand, the rise in oil prices has moderated, reversing the upward trend in inflation in the Dominican Republic (DR). On the other hand, the process of normalization of the monetary policy of the United States has become more gradual and it is expected that the Federal Reserve would maintain an accommodative position for the rest of the year. In addition, the International Monetary Fund (IMF) downgraded US growth prospects to 2.1% in 2017 and 2018, arguing that there would be no fiscal stimulus in the short term.

In terms of the Euro Zone, the IMF projected a growth of 1.9% in 2017 and 1.7% in 2018. On the other hand, Latin America would come out of recession, with the exception of Venezuela, registering moderate growth rates of 1.0% in 2017 and 1.9% in 2018.

In the domestic level, preliminary figures during the second quarter of the year indicate that economic growth was significantly below its potential, influenced by a sharp slowdown in private investment and an important reduction in public spending, particularly in capital expenditure, which has contributed to the non-financial public sector deficit (SPNF) being -0.5% of GDP in May. In addition, monetary aggregates and total loans to the private sector moderated their expansion due to a reduction in both the demand for money and the demand for credit, associated with the influence of external and internal factors on the expectations of private agents.

In this context, the Central Bank of the Dominican Republic reduced its legal reserve requirement coefficient by 2.2 percentage points, as a way of stimulating economic activity through credit in an environment of inflation below the lower limit of the target range. It is expected that this set of monetary measures will contribute to the economic growth, resuming its expected dynamism and that inflation would be around the lower limit of the target range of 4% ± 1% established in the Monetary Program of 2017.

With respect to the external accounts, the activities that generate foreign exchange continue to perform favorably, contributing to maintain the current account deficit at a low level, while strengthening the international reserves position and allowing relative stability in the foreign exchange market.

The Central Bank of the Dominican Republic reaffirms its commitment to conduct monetary policy to achieve its inflation target and maintain macroeconomic stability. In this regard, it will continue to monitor the evolution of the world economy and the domestic situation in order to take the necessary measures in view of possible risks to price stability and the proper functioning of the financial and payment systems.

Santo Domingo, July 31, 2017