

## Statement of the Monetary Policy Committee 20 August 2014

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to keep the Bank's interest rates unchanged.

According to the Bank's updated forecast, published today, the outlook for the real economy over the next three years is broadly similar to that described in the May issue of *Monetary Bulletin*. However, the outlook is for slightly stronger growth in domestic demand this year and throughout the forecast horizon.

The inflation outlook has improved somewhat since May, and it now appears that inflation will remain close to target during the forecast horizon. A positive output gap is forecast to develop later than was assumed in the last forecast and will be less pronounced. Inflation expectations have changed little in the recent past, and long-term expectations are still above target.

The Bank's foreign exchange transactions in the past year have contributed to greater exchange rate stability. This year the Bank has bought significantly more foreign currency than it has sold, in both regular and *ad hoc* purchases. The Bank intends to continue its regular purchases in the current amount as long as conditions remain relatively unchanged. As before, the Bank will intervene in the foreign exchange market as needed to mitigate exchange rate volatility.

The slack in the monetary policy stance has probably disappeared, and it appears, based on the Bank's baseline forecast, that the current interest rate will suffice to keep inflation at target. Robust growth in domestic demand in the near term and growing tension in the labour market could generate increased inflationary pressures, however, and necessitate an increase in the Bank's nominal interest rates.