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Monetary Policy

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Inflation Report no. 1, 2022

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Summary

In the fourth quarter of 2021, the annual inflation rate continued, at a faster pace than expected (Inflation Report no. 4, 2021), the upward trajectory observed since the first part of 2021. Thus, it increased from 6.7% in September 2021 to 13.9% in December 2021. As a result, in the fourth quarter of 2021 it was above the upper limit of the range of 5.0% ±1.5 percentage points. At the same time, the average annual inflation rate in the fourth quarter of 2021 was 11.7%, 6.8 percentage points higher than in the previous quarter. The acceleration of prices in the above-mentioned period was due to the increase in prices for food, oil, natural gas and other raw materials on the international market, which was partly reflected in the increase in the prices of these products on the local market, but especially in adjusting gas and heat tariffs in November 2021. At the same time, rising inflation was supported by persistent demand pressures in the context of increasing disposable income of the population. The inflationary pressures associated with the above-mentioned factors were slightly attenuated by the exchange rate dynamics.

Over the next period, the upward trajectory of the annual CPI rate will continue as a result of rising food and other raw materials prices in the regional market. A pronounced impact on the CPI is to be determined by the full reflection of tariff adjustments by the NBS in the first part of 2022. The increase in gas and heat

tariffs, the further increase in import prices for gas, as well as possible increases in other tariffs will lead to upward pressure on prices on several subcomponents of the CPI. As in previous periods, the subsequent dynamics of the CPI remain marked by the uncertainty of the timing and magnitude of some tariff adjustments in the context of the sharp rise in energy prices in the regional market, but also by the impact of weather conditions on food prices in the internal market.

The year 2021 ended on a negative note, the world economy being affected both by the continuation of the COVID-19 pandemic and by the increase of pro-inflationary pressures. In November 2021, the Omicron variant of the SARS-CoV-2 virus was detected, which spread rapidly worldwide, leading to new social and economic constraints. At the same time, production costs have continued to rise, given that world supply does not meet consumer demand. This has led several countries to take pro-inflationary pressures into account and take steps to counter them. The Federal Reserve has decided to increase rates more substantially and faster, with the average forecast anticipating three increases in 2022. This led to an appreciation of the US dollar, especially against the euro, given the delay in the ECB's reaction to the 5.0% annual inflation in the euro area in December 2021. The escalation of geopolitical tensions over the Ukraine-Russia conflict has led to the depreciation of both the Ukrainian hryvnia and the Russian ruble. The US Congress is currently preparing a new package of economic sanctions for Russia. Oil prices have risen sharply because OPEC+'s ability to increase oil production is limited in the short term and a prompt response to rising world oil demand is not possible. Gas prices in Europe rose sharply in mid-December 2021 after Gazprom no longer reserved transit capacity through Poland. It later became known that demand in Asia had fallen, and that more shale gas vessels in the United States had been relocated to European ports, so that natural gas prices had fallen. Concerns over a possible currency crisis in Turkey have risen in the region, but measures taken by President Recep Tayyip Erdogan have raised short-term confidence in the Turkish lira and the government's ability to handle rising prices.

After the sharp acceleration of April-June 2021, economic activity continued the positive dynamics, but at a more modest pace. The positive evolution was supported, mainly, by the domestic demand from the population and the positive economic dynamics in the region. Thus, in the third quarter of 2021, GDP was 8.3% higher than in the similar period of 2020, the respective dynamics being, however, lower than the one anticipated in the Inflation Report no. 4, 2021. At the same time, the seasonally adjusted series reflects a 3.3% decrease in GDP compared to the second quarter of 2021. In this context, according to estimates, the effect of aggregate demand on prices was less pronounced than anticipated in the Inflation Report no. 4, 2021. The positive dynamics of GDP was mainly due to the increase in household consumption and exports. However, a significant part of the domestic demand led to an increase in imports, which attenuated the domestic economic dynamics. On the supply side, more significant positive developments were recorded in agriculture, trade and industry. The sharp increase in economic 4 Inflation Report, February 2022 (National Bank of Moldova) activity was partly reflected in the dynamics of labor market indicators. Thus, in the third quarter of 2021 both the economically active and the employed population registered an increase compared to the similar period of the previous year. At the same time, the unemployment rate as well as the underemployment rate registered a downward dynamics. Most of the operational indicators available in October and November 2021 continued to show pronounced positive developments, but overall less intense compared to those of the third quarter of 2021, thus outlining prospects for a positive GDP dynamics at the end of 2021.

In the fourth quarter of 2021, the revenues of the national public budget recorded increases, being by 29.3% above the level recorded in the similar period of 2020. Expenditures of the national public budget increased, being 9.4% above the level recorded in the fourth quarter of 2020. At the same time, on the state securities market, allocated during the fourth quarter of 2021, interest rates remained on the upward trend.

In the fourth quarter of 2021, excessive liquidity amounted to 3.6 billion lei, decreasing compared to the previous quarter by 0.7 billion lei.

Monetary aggregates in the fourth quarter of 2021 registered a positive dynamic in annual terms. At the same time, the main contribution to this development was largely due to the change in the volume of deposits in national currency and in foreign currency.

During the fourth quarter of 2021, three meetings of the Executive Board of the National Bank of Moldova on monetary policy decisions took place. Following the assessment of the balance of internal and external risks and the short- and medium-term inflation outlook, the Executive Board of the National Bank of Moldova decided to increase the base rate applied to the main monetary policy operations by 1.85 percentage points to 6.50% annually.

The average interest rates on the balance of loans in national currency increased by 0.12 percentage points compared to the previous quarter, those on the balance of deposits increased by less than 0.03 percentage points. Average interest rates on loans and foreign currency deposits continued their downward trend.

Recent developments indicate the persistence of external pro-inflationary pressures. Oil prices are hovering around USD 90/barrel, and some experts predict that USD 100/barrel for Brent oil will be reached soon. European gas quotations remain at very high levels, and recent events have shown the fragility of the energy system to supply shocks. The precarious harvest of certain crops and the increase of logistics, transport, energy and financing costs will continue to contribute to the increase of quotations for food products on the international market in 2022, which will gradually moderate towards 2023. In order to counter pro-inflationary pressures, it is expected that emerging economies will continue and advanced ones will begin to tighten monetary conditions.

The annual inflation rate will increase rapidly by the third quarter of 2022, then decline sharply by the end of the forecast horizon[1] . The annual inflation rate from the first quarter onwards will continue to be above the upper limit of the range and will return only in the second quarter of next year.

The annual rate of core inflation will have an upward trend during the current year, subsequently decreasing continuously until the end of the forecast period[2] . The annual pace of food prices will continue to increase significantly in the first quarter of 2022, after which it will decrease significantly until the end of the forecast period[2]. The annual rate of regulated prices will continue to increase sharply until the second quarter of this year, after which it will decrease rapidly. From the second quarter of next year until the end of the forecast horizon, it will record negative values. The annual rate of fuel prices will slow down considerably over the entire forecast period.

Aggregate demand will also increase in positive terms in the first quarter of the forecast, after which it will continue to decline, but will be pro-inflationary over the entire forecast horizon. This trajectory will be largely supported by a positive fiscal momentum, a revival of external demand and stimulating interest rates, although overall monetary conditions will be restrictive.

Real monetary conditions will be restrictive over the entire forecast period, with a negative impact on aggregate demand. The current inflation forecast, compared to the previous inflation report, has been significantly revised upwards over the entire comparable period[3] . The current forecast for the annual rate of core inflation has increased considerably over the entire comparable period. The annual rate of food prices has been reconfigured, revised upwards for the first quarter of 2022 and the last two quarters of the

comparable period. Starting with the second quarter of 2022, for four consecutive quarters, the annual rate of food prices has been revised downwards. The current forecast of the annual rate of regulated prices has been significantly revised upwards for the comparable period, except for the last two quarters. The forecast for the annual rate of fuel prices was increased for the entire comparable period.

Most central banks continue to raise monetary policy rates. Thus, between February 1-11, 2022, the following monetary authorities increased the monetary policy rates: The Central Bank of Armenia increased its refinancing rate from 7.75 to 8.0% on February 1 (+0.25 percentage points), and the Bank of England on February 3 increased the base rate from 0.25 to 0.5% (+0.25 percentage points), the National Bank of the Czech Republic on February 3 increased the two-week repo rate from 3.75 to 4.50% (+0.75 percentage points), on February 4, the National Bank of Poland increased the reference rate from 2.25 to 2.75% (+0.5 percentage points), the Central Bank of Iceland on February 8 increased the key interest rate from 2.0 to 2.75% (+0.75 percentage points), the National Bank of Romania on February 9 increased the monetary policy interest rate from 2.0 to 2.5% (+0.5 percentage points), the Bank of Russia on February 11 increased the base rate from 8.5 to 9.5% (+1.0 percentage points).

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1. Quarter IV 2023
2. Quarter I 2022 – quarter IV 2023.
3. Quarter I 2022 – quarter III 2023.

See also

Tags
Rata anuală a inflației [2]
core inflation [3]
External environment [4]
inflation forecast [5]
forecast [6]
forecasting inflation [7]

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