12.11.2024

Inflation Report no. 4, 2024

NBM Governor Anca Dragu presents the Inflation Report No. 3, 2024

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Summary

Inflation

In the third quarter of 2024, the annual inflation rate followed an upward trajectory after the downward trend that began at the end of 2022. As a result, the annual inflation rate increased from 3.8% in June 2024 to 5.2% in September 2024, placing it within the variation range of the inflation target. At the same time, the average annual inflation rate was 5.0% in the third quarter of 2024, about 1.5 percentage points higher than in the previous quarter. The upward trajectory of the annual inflation rate was supported by some adverse sectoral developments, including dry conditions in the summer of this year, which caused food prices to rise. These were slightly mitigated by the effect of moderate domestic demand. Insignificant pressures continued to be exerted by food prices on the international market and by industrial production prices on the domestic market. Disinflationary pressures were driven by global oil prices. In the reference quarter, the annual rate of the CPI was lower than the one anticipated in the previous forecasting round (Inflation Report, August 2024), mainly due to the negative deviation recorded for the forecast of the annual rate of regulated prices.

Recently, prices in industry have fallen, setting the stage for a moderation of price pressures on certain subcomponents of the CPI in the period ahead. In addition, domestic demand will continue to exert a disinflationary impact in the coming period, which could, however, be mitigated by some tariff adjustments. Nevertheless, in the upcoming period, the annual

CPI rate will remain within the variation range from the target. The manner in which tariffs are adjusted, as well as the tense situation in the region and the risks of its escalation, keep the inflation outlook highly uncertain.

External environment

The global economy in the second half of the current year continued to oscillate between trade and geopolitical tensions and the beginning of monetary policies easing in the USA and the euro area. During the reference period, alongside the additional sanctions against the Russian Federation, reciprocal trade tariffs were imposed between the EU and China. Geopolitical tensions escalated after the invasion of Russian territory in the Kursk region by Ukrainian troops and the intensification of bombings in the Middle East. At the monetary policy meeting in September 2024, the FRS lowered the interest rate range by 50 basis points. The ECB also decided at its monetary policy meeting on September 12, 2024, to reduce the deposit facility interest rate by 25 basis points. At the same time, the decision to decrease the spread between the interest rate on the main refinancing operations and the deposit facility interest rate from 25 to 15 basis points also came into effect. On October 23, 2024, the ECB cut interest rates again by 25 basis points. Oil prices hit their lowest level of the year in September 2024 amid concerns about declining demand in China. However, in early October 2024 they returned to previous levels due to heightened tensions in the Middle East. The price of natural gas in Europe also increased, amid concerns about the expiration of the contract of the natural gas transit through Ukraine at the end of 2024, although natural gas reserves in Europe are at record levels for this period. Also, in September 2024, for the first time since the end of 2022, a positive annual growth rate was recorded for the FAO index of agricultural and food prices on the international market, signaling a reversal of the trend.

Economy

In the second quarter of 2024, GDP continued its positive momentum since the beginning of this year. Thus, in the second quarter of 2024, GDP increased by 2.4% compared to the same period of 2023. However, this dynamic was lower than the one anticipated in the Inflation Report, August 2024. The upward trajectory of GDP was mainly supported by domestic demand, both from the population, in the context of real income growth, and from economic agents. Net external demand had a negative impact on GDP dynamics during this period. At the same time, some more pronounced positive developments in trade sector, financial and insurance activities, information and communication sector, and construction are worth mentioning. On the one hand, the agricultural and industrial sectors had a minor impact on GDP dynamics, while on the other hand, real estate transactions and transport and storage sector had a negative impact on the GDP trajectory. According to estimates, domestic demand continued to be moderate, signaled by the lower-than-expected development in household consumption, thus having a disinflationary impact. At the same time, the seasonally adjusted series reflects an 0.4% increase in GDP compared to the first quarter of 2024. Overall, GDP increased by 2.2% in the first half of the year compared to the same period of the previous year.

Monetary policy

In the third quarter of 2024, excess liquidity amounted to MDL 9.6 billion, down by MDL 355.3 million compared to the previous quarter.

The M3 monetary aggregate, in the third quarter of 2024, recorded an annual growth rate of 17.1%, with the main contribution coming from the balance of deposits in the national currency.

During the third quarter of 2024, two meetings of the Executive Board of the National Bank of Moldova were held on monetary policy decisions. Following the assessment of the internal and external balance of risks and the inflation outlook in the short- and medium-term, the Executive Board of the National Bank of Moldova, at its meetings on August 6, 2024 and September 19, 2024, decided to maintain the base rate at the level of 3.60% annually (level set on May 7, 2024). At the same time, standing facility and repo rates were also maintained at their current levels. The required reserves ratio of funds attracted in MDL and non-convertible foreign currency and that of funds attracted in freely convertible foreign currency remained unchanged. These measures were adopted with the aim of stimulating aggregate demand, including by encouraging consumption, balancing the national economy and anchoring inflationary expectations.

At the same time, during the ordinary monetary policy meeting on November 5, 2024, the Executive Board of the National Bank of Moldova adopted, by an unanimous vote, the decision to maintain the base rate at the level of 3.60% annually, respectively the rates on standing facilities and repo operations were maintained. At the same time, the required reserves ratio of funds attracted in MDL and non-convertible foreign currency and that of funds attracted in freely convertible foreign currency was lowered starting with the period of application of required reserves from November 16, 2024, to December 15, 2024, to the levels of 27.0% and 36.0% of the calculation base, respectively.

This decision was taken in the context of further spillovers from previous monetary policy decisions, given the lags in their transmission. At the same time, the decision aims at lowering borrowing costs and thereby further supporting private sector lending and boosting the national economy.

The cumulative monetary policy stimulus measures, both the consecutive cuts in the base rate and the lowering of the required reserves ratio, will increase excess liquidity in the banking system by the end of this year. The current and projected volume of liquidity will allow banks to lend to economic agents and households, as well as to invest in state securities (SS).

In the third quarter of 2024, within the national currency segment, the weighted average interest rates on new loans and on term deposits continued their downward trend under the impact of the cumulative monetary policy stimulus measures. Thus, the weighted average rate on loans amounted to 8.63% and that on deposits – 3.12%, down by 2.75 and 1.49 percentage points, respectively, compared to the third quarter of 2023.

The average interest rates on the balance of loans in national currency decreased compared to the third quarter of 2023 by 1.91 percentage points to 8.81%, and on term deposits – by 5.95 percentage points, reaching 3.51%.

Medium-term inflation projection

In the current forecast round, the external environment continues to present heightened risks and uncertainties, but overall, external assumptions are shaping the current trajectories. On the one hand, the disinflationary pressures related to falling prices have dissipated, and now a cycle of slight price increases is expected on the international market. On the other hand, global consumption continues to be weak, affecting production and costs. The effect of rising real household incomes and results from services activity will continue to be a driver of economic growth. The volatility of financial and commodity markets will be susceptible to geopolitical tensions in the Middle East and Ukraine, as well as to the outcome of the USA presidential elections.

The annual inflation rate will continue to rise slightly until the beginning of next year, thereafter, towards the end of the forecast horizon, it will show a downward trend[1], except for the fourth quarter of 2025, when it will increase slightly. Over the entire forecast period[2], the annual inflation rate will be positioned close to the target of 5.0% and will remain within the variation range throughout the forecast horizon. The annual core inflation rate will continue its downward trajectory until the first half of next year, after which it will fluctuate slightly until the end of the forecast horizon. The annual rate of food prices will increase until the beginning of next year, after which it will decline towards the end of the forecast horizon. The annual rate of regulated prices will continue to increase until the second quarter of the forecast, thereafter it will show a downward trend until the third quarter of 2025, followed by an increase towards the end of the forecast horizon, except for the last two quarters. The annual growth rate of fuel prices will continue to decline slightly and register negative values in the first quarter of the forecast period, thereafter it will rise continuously and, starting from the second half of next year, it will be close to zero by the end of the forecast period.

Negative aggregate demand over the entire forecast horizon will be driven by dry conditions in the summer of 2024, the cumulative real appreciation of the national currency, and relatively weak external demand in the current and early next year. The low real interest rate and positive fiscal impulse over the forecast period, the recovering and subsequently positive external demand from the fourth quarter of 2025 until the end of the forecast horizon will narrow the aggregate demand deficit.

Real monetary conditions will have a restrictive effect on domestic demand throughout the entire forecast horizon.

The current inflation forecast, compared to the one in the Inflation Report, August 2024, has been revised downward over the comparable period[3]. The annual core inflation rate has been adjusted downward for the entire comparable period. The current forecast of the annual rate of food prices has been increased until the first half of 2025 and decreased for the remainder of the comparable period. The annual rate of regulated prices has been revised downward until the third quarter of 2025 and upward towards the end of the comparable period. The forecast for the annual rate of fuel prices has been lowered for nearly the entire comparable period.

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1. Third quarter of 2026

2. Fourth quarter of 2024 – third quarter of 2026

3. Fourth quarter of 2024 – second quarter of 2026

See also

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