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Monetary Policy

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Inflation Report no. 1, 2013

Inflation Report no.1, February 2013 [1]

Summary

Inflation developments

The annual rate of inflation was 3.9 percent in the fourth quarter of 2012, by 0.5 percentage points lower than the previous quarter. The downward trend was due to the decrease of pressures from regulated prices with the gradual elimination of the impact of tariff increases of gas and heating operated in the fall of 2011 from their annual measure. The drought in 2012 led to an increase in pressure from food prices, so that by the end of 2012 the annual inflation rose to 4.1 percent. The annual rate of core inflation in the fourth quarter of 2012 marked the end of a downward trend that lasted more than a year, so it was 3.7 percent in December 2012. However, the average core inflation continues to be lower than the previous quarter due to a moderate domestic demand in 2012. The evolution of the inflation annual rate in the fourth quarter of 2012 was slightly lower (by 0.2 percentage points) than the expected value in its projection (4.1 percent) of the Inflation Report no. 4, 2012. In the fourth quarter of 2012, the annual rate of industrial production price index was 4.8 percent, down by 0.2 percentage points from the previous quarter. At the same time, the annual rate of construction prices was 8.7 percent, thus representing the end of the upward trend started in 2010.

External environment

The transition from 2012 to 2013 in the global economy combines complex issues' consequences that dominated the international financial markets in 2012 and the challenges for the economies in 2013 to achieve the potential growth level. The peak of the euro area sovereign debt crisis seems to be overcome, the European economies orienting themselves in 2013 towards economic recovery, although it will be dampened by austerity measures adopted by most member states. The U.S. economy evolves satisfactorily, the problems of fiscal policy remains to be factor that may cause damage. The emerging economies continue to be clearly affected by the reduction of international trade and international prices of main commodities have a tendency to diminish slightly.

Economic developments

Preliminary data presented by the National Bureau of Statistics confirmed the expectations made in October on the evolution of GDP in the third quarter of 2012. Thus, its annual growth rate has turned negative, constituting minus 1.7 percent, as a result of pronounced negative developments in the agricultural sector caused by drought, but also by a less favorable external environment, in particular by the contracting

European economy.

Household consumption growth registered a value of only 1.0 percent in the context of a tempered development in its disposable income. General government final consumption recorded an increase of 1.4 percent compared to the third quarter of 2011. Gross fixed capital formation dynamics was slightly more pronounced in the third quarter than in the second quarter, increasing by 0.8 percent, driven by increased spending for capital repairs of fixed assets, while capital investments have contracted. Exports and imports recorded increases of 1.9 percent and 3.1 percent, respectively, much lower values than in previous periods.

The value added of agriculture registered a decrease of 30.8 percent while the industry grew slightly in all sectors. At the same time, services' gross value added recorded an increase of 4.1 percent, mainly due to the development of trade, transport and communications. In the third quarter of 2012, the unemployment rate was 4.8 percent, decreasing compared to the same period of 2011. However, the number of employed decreased by 4.0 percent compared to the third quarter 2011.

Monetary policy

During the fourth quarter of 2012, the NBM adopted three decisions to maintain the monetary policy interest rate at the level of 4.5 percent annually. The major argument of those decisions was the strengthening of the disinflation trend in the Republic of Moldova.

During the fourth quarter of 2012, the NBM intervened in the domestic foreign exchange market as a buyer of foreign currency in the context of the monetary policy promoted by it and in order to ensure the consolidation of foreign exchange reserves.

During the analyzed period, the volume of NBM transactions carried out on the domestic foreign exchange market against MDL constituted USD 71.27 million. From the beginning of 2012, the monetary indicators recorded a pronounced growth. Thus, in the fourth quarter of 2012, the growth rate of monetary aggregates has increased, the quarterly average in annual terms constituting 22.7 percent for M2 and 18.6 percent for M3, by, respectively, 4.8 percentage points and 4.4 percentage points more as compared to the previous quarter.

The average interest rates charged by banks in the fourth quarter of 2012 had a stable evolution, registering significant increases or decreases. In late December 2012, the average interest rate on new loans in national currency recorded a new historical minimum of 11.98 percent, and those in foreign currency - 8.32 percent. In turn, bank term placements returns have been higher than the previous quarter values both in national and in foreign currencies.

Medium-term inflation forecasting

Throughout the forecasting period, the annual inflation rate will fall within the range of variation of ± 1.5 percentage points from the target, and in 2014 it will be close to its lower limit. Although the inflation is projected on a tolerable area, it will mostly be in the bottom half of the range of variation. The moderate economic growth will generate disinflationary pressures from aggregate demand. Thus, during the forecast period, the supply-side inflationary pressures will persist. In such circumstances, the expansionary condition of the monetary policy, both now and for the forecasting period, is understandable.

Compared with the previous forecast, the annual inflation trajectory will be lower throughout 2013, the biggest difference being in the second quarter of 2013. During 2013, the annual inflation rate will be lower on average by about 1.3 percentage points compared with the previous forecast. Next year, the average inflation rate will be around 3.7 percent.

The current round of forecasting anticipates a negative quarterly dynamics for the output gap in the quarters I - III of 2013, with a modest recovery to positive territory in late 2013 and throughout 2014. The recovery rates are modest, placing the economic activity below its potential level, thus exerting disinflationary pressures from the demand side. The latter is caused by the contraction of external demand and an agricultural year severely affected by adverse weather conditions.

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