06.08.2024

Monetary Policy Decision, 06.08.2024

At its meeting held on 6 August 2024, the Executive Board of the National Bank of Moldova unanimously adopted the following decision:

1. **to maintain the base rate applied to the main short-term monetary policy operations at 3.60 percent annually.**
2. **to maintain interest rates as follows:**
   a) on overnight loans, at 5.60 percent annually;
   b) on repo operations, at 3.85 percent annually;
   c) on overnight deposits, at 1.60 percent annually.
3. **to maintain the required reserve ratio of funds attracted in MDL and non-convertible foreign currency at the current level of 29.0 percent of the calculation basis.**
4. **to maintain the required reserve ratio of funds attracted in freely convertible foreign currency at the current level of 39.0 percent of the calculation basis.**

The NBM's Executive Board also approved today the Inflation Report of August 2024, which will be published on 13 August 2024.

This decision is taken in the context of the ongoing effects of previous monetary policy decisions, given the lags in their transmission.

The current assessment of real monetary conditions in the deposit, credit, and foreign exchange markets points to a favourable situation for keeping inflation within ±1.5 percentage points of the 5.0 percent medium-term target.

Recent macroeconomic information mainly confirms the main assumptions and conclusions reflected in the Inflation Report of May 2024.

Inflation. Annual inflation was 3.8 percent in June 2024, 0.1 percentage point below the March 2024 level. In June this year, the annual inflation rate returned to the ±1.5 percentage point corridor from the 5.0 percent target after temporarily exceeding it in May. The downward movement in the annual inflation rate in the second quarter of 2024 was driven, on the one hand, by the modest domestic demand and, on the other hand, by the trajectory of international food prices, domestic agricultural and industrial output prices, as well as fuel and regulated prices. It should be noted that aggregate demand continues to have a modest disinflationary impact on the annual inflation rate, which will be mitigated by some tariff adjustments, such as the increase in healthcare tariffs that took effect in July this year. In the second quarter of 2024, the annual inflation rate was 3.5 percent, 0.5 percentage points lower than anticipated in the forecast of the Inflation Report of May 2024, mainly due to the negative deviation in the fuel price forecast.

External Environment. Global economic activity strengthened at the start of the year, moving toward its potential. The euro area economy is recovering, the unemployment rate is at historically low levels, and annual inflation eased to 2.5 percent in June 2024. Inflationary risks remain elevated, raising the prospect of higher interest rates for longer periods amid escalating trade tensions and geopolitical uncertainties. After the resumption of gas deliveries from Norway, the price of natural gas in Europe fell back to the range of USD 300-400 per 1,000 cubic meters established earlier this year. Oil prices continued to fall due to weak global demand and rising oil inventories. However, the Brent quotation remained above USD 80 per barrel. The FAO International Food Price Index was unchanged in June 2024 from May 2024.

Economic Activity. Data released by the NBS for the first two months of Q2 2024 show mixed trends in economic activity. Thus, exports contracted by 12.7 percent annually between April and May 2024, while the annual rate of imports increased by 4.95 percent. Retail trade and wholesale trade grew on average by 22.0 and 10.7 percent annually, respectively. Industrial production averaged -0.1 percent. According to estimates, GDP is projected to continue its positive dynamics in the second quarter of 2024.

Monetary Conditions. Excess liquidity in the banking sector, although slightly decreasing compared with the second quarter of 2024, amounted to MDL 10.0 billion, which is sufficient to maintain lending in the immediate period ahead. The cumulative monetary policy stimulus measures led to a continued decline in interest rates on new loans and deposits in MDL in the second quarter of 2024. Thus, the weighted average interest rate on loans amounted to 9.08 percent, and that on deposits to 3.24 percent, down by 4.1 and 4.05 percentage points, respectively, compared with the second quarter of 2023. The consecutive reduction in interest rates led to an increase in the volume of new loans granted in MDL by 51.4 percent annually in the second quarter of 2024. This dynamic was driven by the increase in loans granted for both consumption and real estate to individuals and to legal entities in the trade sector.

Forecast Update. The annual inflation rate will trend relatively stable over the forecast period. Thus, the average annual inflation for the years 2024 and 2025 will be 4.7 and 5.3 percent, respectively, revised by -0.3 and 0.7 percentage points, respectively. The current inflation forecast has been revised downward for the second half of this year and upward for the second quarter of 2025 through the first quarter of 2026. The downward revision of the annual inflation forecast is largely driven by a lower forecast for international food and oil prices. As for the upward revision, it is conditional on the impact of dry weather conditions in the summer of 2024 on food prices in the first half of 2025, expectations of less restrictive aggregate demand over the whole comparable period, and a higher forecast for natural gas prices. It should be noted that the cumulative monetary policy stimulus measures of both consecutive cuts in the base rate and a lowering of the reserve requirement 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 finance the budget deficit.

Risks and Uncertainties. However, some risks and uncertainties to the medium-term inflation outlook persist, such as disinflationary aggregate demand, the vulnerability of domestic fruit and vegetable prices to weather conditions in the period ahead, uncertainties about the volume of agricultural production in 2024 and 2025, the evolution of regulated prices, the tense regional and global situation, the volatility of expectations regarding international commodity quotations, and the EUR/USD parity. **Therefore, although there are risks to the evolution of the annual inflation rate, it will remain within the variation range during the forecast horizon**.

The NBM's decision comes in the context of existing monetary conditions that are conducive to keeping inflation within ±1.5 percentage points of the target of 5.0 percent, a level considered optimal for the growth and economic development of the Republic of Moldova in the medium term.

The next meeting of the Executive Board of the NBM on monetary policy will take place on 19 September 2024, according to the approved schedule [1].

NBM Interest rates [2]

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