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Politica monetară

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Inflation Report no. 2, 2018

Inflation Report no. 2, May 2018 [1]

Summary

The annual inflation rate will gradually decrease within the set variation interval, but will return to the target level in the second half of 2019. Core inflation will continue to decrease throughout the year, after which, in the second half of the next year, it will return close to 5.0% level. The growth rate of food prices will drop significantly over this year, however, the trend is expected to reverse in the coming year. The same downward trend will be recorded for regulated prices, which are expected to fall in the current year to about -4.0%. The annual growth rate of fuel prices will have a downward trajectory, which will be followed by a slight increase at the beginning of the forecast horizon.

Aggregate demand will maintain a disinflationary trend over the next two years, largely due to existing monetary conditions, the economic cycle, as well as internal and external factors. Strong appreciation of the actual real exchange rate will continue exerting pressures on the competitiveness of domestic products with a corresponding impact on the trade balance. At the same time, through another channel, the appreciation will largely offset this effect, by lowering the costs of imported components, decelerating the CPI and by generating pressures that will enhance productivity.

The Real Monetary Conditions Index denotes a restrictive character of monetary conditions throughout the forecasting period. At the same time, disinflationary pressures of the current year, which are to be followed by pro-inflationary pressures of the coming year, suggest that a marginal relaxation of monetary policy is not sufficient. In the short term, the seasonally adjusted currency supply will determine the exchange rate.

In line with the Budget Law for 2018, the tax policy will stimulate economic activity throughout this year, the slowing down of fiscal impulse being forecasted for the next year.

Global macroeconomic activity records positive trends, however, is associated with many risks and uncertainties. The escalation of diplomatic and geopolitical conflicts have determined an increased volatility of the main macroeconomic indicators. The protectionist measures, promoted by the US President Donald Trump, as well as the threats of countermeasures to be taken by the US trading partners, gave rise to apprehensions that a large-scale trade war may commence, that will develop along the US-China axis. The worsening of diplomatic relations between London and Moscow and the new US sanctions imposed on 6 April 2018 against Russian billionaires hit the Russian ruble and the Russian stock market. International oil prices have increased following the output cuts, which exceeded the levels agreed by the OPEC (+) members, but also following the escalation of the geopolitical conflict in Syria. At the same time, there are the first scattered signs of the slowing down of global economy's growth rate, which may be a negative factor for global economic growth, given the rise in commodity prices and the intensification of risks.

The latest inflation forecast remains quite close to the initially projected values, although they were slightly revised downwards for the current year. The core inflation was revised downwards throughout the forecasting period following the aggregate demand's revision. The forecast for the growth rate of food prices was revised upwards being mainly driven by the upward revision of the forecast for international food prices. The forecast for the growth rate of regulated prices was revised downwards for the current year and upwards for the next year. The forecast for the growth rate of fuel prices has been slightly revised due to rising oil prices as well as the strengthening of the exchange rate of domestic currency.

In the first quarter of 2018, the CPI annual rate recorded a downward trend, which was mainly driven by the dynamics of regulated prices, being also supported by the trend towards appreciation of domestic currency. Thus, annual inflation decreased from 7.3% in December 2017 to 4.7% in March 2018. According to estimates, domestic demand has continued to exert a negligible impact on inflation through the beginning of this year. Strong pressures, generated by food prices last year, are gradually losing intensity. At the same time, the adjustment of excise duties and the rise in international oil prices, as well as their impact over local fuel prices, were mitigated by the exchange rate dynamics. Since January, the CPI annual rate has been within the inflation target range set in the medium-term monetary policy strategy. Similarly to the preceding periods, the annual inflation rate remained within the inflation target limits set in the Inflation Consultation Mechanism under the IMF Memorandum. The CPI annual rate recorded lower values than were projected in the previous forecasting round due to a lower-than-expected gas supply tariff set for 2018 and a stronger exchange rate. In the second quarter of 2018, the CPI annual rate is expected to record a sharper decline, being largely driven by such factors as the anticipation of a lower electricity tariff, the appreciation of domestic currency, a still modest domestic demand, and the slowdown of the growth rate of food prices compared to the same period of the previous year. Industrial prices have recorded a downward trajectory in the first three months of 2018, thus outlining the first signs of a future decline in some of the CPI subcomponents.

In the fourth quarter of 2017, the annual growth rate of economic activity accelerated compared to the first half of 2017, being driven by both the growth of aggregate demand and the agricultural performance. Thus, in the fourth quarter of 2017, GDP \acs{PIB} grew by 6.4% compared to the same period of 2016. The contribution generated by household consumption marked a significant increase compared to previous quarters, recording the annual growth rate of 5.8%. The public administration consumption recorded slightly negative dynamics. In the fourth quarter of 2017, a positive, though smaller than in the previous quarter, contribution to the dynamics of economic activity was generated by the investment component. As a result, gross fixed capital formation increased by 5.9%. Besides, a strong positive contribution to GDP growth was generated by exports. Thus, in the fourth quarter of 2017, exports recorded values 12.4% higher than in the same period of the previous year.

However, an important part of positive contribution generated by the above-mentioned components was offset by the increase in imports by 8.0%. This development was driven by the increase in domestic demand, as well as by the appreciation of domestic currency against the US dollar. By resources categories, GDP growth, in the fourth quarter of 2017, was mainly driven by a positive contribution from agriculture and net product taxes. Positive, yet smaller, contributions were generated by the increase in gross value added of trade, industry and transport and storage. Agricultural performance has determined the increase in the employment rate in the national economy. Most economic indicators of the first quarter of 2018 outline preconditions for a strong economic growth in the reporting period and a slowdown of economic activity in the second half of the year.

In the first quarter of 2018, the annual growth rate of public budget expenditure recorded a notable downward trend, decreasing by 0.9% compared to the same quarter of 2017. This trajectory could create negative pressures on domestic demand in the coming months. At the same time, these pressures may be mitigated by positive developments in public budget revenues. It should be noted that at the end of the first quarter of 2018, for the first time in the history of the Republic of Moldova, the Ministry of Finance issued government bonds with five-year maturity. This financial tool will be used regularly, starting with the second quarter of this year. Increasing the yield curve is an important step in consolidating the government securities market and the capital market of the Republic of Moldova. Developing the capital market is essential for any economy in order to enlarge access to financing for all economic agents. At the same time, the market conjuncture allowed the Ministry of Finance to continue lowering interest rates on the government securities placed on the market, which decreased, during the first quarter of 2018, for all types of maturities.

In the first quarter of 2018, the volume of excess liquidity continued to rise, recording a record level of 9.6 billion lei. This growth was largely driven by a steady decline in the loan portfolio of the banking system (although new loans recorded an increase) against the background of a moderate loan demand, the tightening of prudential requirements following the recent financial crisis, the monetary issues as a result of the NBM's interventions on forex market, as well as the migration of lending activity outside the banking system. In such conditions, banks preferred to invest in low-risk instruments, such as GS \acs{VMS} and NBC.

In the first quarter of 2018, monetary aggregates recorded positive and faster dynamics compared to the previous quarter. This evolution was largely determined by the increase in sight deposits, which were placed both in domestic and foreign currency.

Following the trend set by the base rate applied to main monetary operations of the National Bank of Moldova and as a result of the liquidity surplus recorded in the banking system, average interest rates of licensed banks continued their downward trend.

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