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Monetary Policy

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Press release of the National Bank of Moldova, 8 August 2016

Within the meeting of the 8 August 2016, the Executive Board of the National Bank of Moldova adopted the following decision by unanimous vote:

1. to maintain the base rate applied on main short-term monetary policy operations at the current level of 10.0 percent annually;

2. to maintain the interest rates:
- on overnight loans at the current level of 13.0 percent annually;
- on overnight deposits at the current level of 7.0 percent annually;

3. to maintain the required reserves ratio from financial means attracted in freely convertible currency at the level of 14.0 percent of the base.

4. to maintain the required reserves ratio from financial means attracted in MDL and non-convertible currency at the current level 35.0 percent of the base;

Executive Board of the NBM approved the Inflation Report no.3, 2016, which will be presented at a press conference on 11 August 2016.

The analysis of the most recent statistic data shows the downward trend of the annual inflation rate for the sixth consecutive month, although it is still above the upper limit of the range of ± 1.5 percentage points from the 5.0 percent target.

The annual inflation rate was 7.4 percent in June 2016 or by 0.5 percentage points less compared to the previous month. This slowdown was mainly due to the decrease of the contributions from food prices and core inflation.

The annual rate of core inflation[1] was 9.3 percent in June 2016, decreasing by 0.5 percentage points compared to the previous month.

The dynamic of macroeconomic indicators in the first two months in the second quarter of 2016 shows positive signals relating to the revival of the economic activity in the reporting period. In April-May 2016, the exports increased by 3.3 percent compared to the same period of 2015, imports by 3.9 percent and industrial production recorded a medium level of 2.0 percent. At the same time, the turnover amount related to retail trade increased on average by 2.2 percent, while that of trade in services decreased on average by 2.5 percent. In the first quarter of 2016, global agricultural production increased by 4.1 percent compared to the same period last year.

In terms of consumer demand, the annual average real wage growth in the economy in April - May 2016 was minus 0.1 percent, by 1.7 percentage points higher than in the first quarter of 2016. Money transfers to

individuals through the banks of the Republic of Moldova fell by 8.4 percent in January-June 2016 and in nominal terms by 11.9 percent in June 2016, compared with the same periods of 2015.

In the second quarter of 2016, lending and saving processes recorded different developments. The volume of new loans granted during the reporting period decreased by 15.8 percent, while new attracted deposits increased by 31.5 percent compared to the same period of last year. The total balances of loans and deposits decreased at the end of June 2016 by 12.7 percent and 0.3 percent, respectively, compared to the same period of last year.

The average rate of new loans granted in national currency decreased by 1.38 percentage compared to the level recorded in March 2016, accounting for 14.15 percent. The rate of new deposits attracted in MDL decreased in June 2016 by 3.98 percentage points, up to the level of 10.71 percent.

According to the new round of forecasting, the annual average inflation rate will reach in 2016 and 2017 the level of 6.7 percent and 4.4 percent respectively, with the return within the range of variation in the third quarter of 2016. NBM decreased the average inflation forecast published in May 2016 by 0.3 percentage points for 2016 and by 0.4 percentage points for 2017, respectively.

The monetary policy continues to be affected by the complexity of risks and uncertainties associated with the development of internal and external environment. The external disinflationary risks associated with the weak economic activity in the Euro area countries and the recession of the Russian Federation - the main trading partners of the Republic of Moldova, with repercussions on short-term decrease in foreign currency income of the households and domestic exporters through the remittances and foreign trade channel. This, in turn, influenced the further inflation development. Potential risks to inflation arise from the increased volatility of the international financial foreign exchange markets. The main internal risks arise from postponing the adjustment of regulated tariffs. At the same time, the existing meteorological conditions favour an increase in agricultural production compared to the previous year, which will influence negatively the growth rate of food prices during two-three consecutive quarters and will determine the further decrease of consumer inflation.

It should be mentioned that the monetary policy measures adopted by the NBM at the beginning of the year are to be transposed into the national economy through various transmission channels, including by influencing interest rates on loans and deposits in national currency, thus exerting further effects on inflation development.

In assessing the inflation outlook in the short and medium term, within the meeting held on 08 August 2016, the members of the Executive Board of the NBM decided by unanimous vote to maintain the policy rate at the current level of 10.0 percent annually.

The decision is aimed at anchoring inflation expectations in the context of restoring and maintaining the inflation rate close to the target of 5.0 percent over the medium-term, with a possible deviation of ± 1.5 percentage points. The gradual calibration of monetary policy conduct, supported by the expectations on inflation rate decrease, aims to ensure adequate real monetary conditions for the stimulation of lending and savings and for boosting the domestic demand, along with further adaptation of domestic economic environment to the volatility and uncertainty related to external environment.

The output gap will remain negative during the further eight quarters and will reach positive values only to the end of forecasting horizon. The evolution of the economic activity mainly below its potential will determine disinflationary pressures from domestic demand, although more moderate compared to the

previous forecasting.

Inflation Report no.3, 2016 includes a more detailed assessment of the macroeconomic situation, inflation forecast in the medium-term and potential risks and challenges that will be faced by the monetary policy in the next periods. The report will be published on 11 August 2016 as scheduled.

NBM will continue to manage firmly the liquidity excess through sterilization operations, according to the announced schedule.

At the same time, National Bank will continue to offer banks liquidity, according to the schedule announced for 2016, through REPO operations with the term of 14 days, at a fixed rate equal to the base rate of the National Bank plus a margin of 0.25 points percentage.

NBM will further monitor and anticipate the domestic and international economic environment developments, including the potential impact of the Brexit vote, so that by the flexibility of operational framework specific for the inflation targeting strategy to ensure price stability in the medium term.

The next meeting of the Executive Board of the NBM on monetary policy will take place on 25 August 2016, according to the announced schedule.

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[1]Core inflation is calculated by the NBS, excluding prices that are outside the influence of monetary policy promoted by the NBM, such as food and beverages, fuel, products and services with regulated prices. Data prepared and published from January 2012 are calculated by the NBS according to the modification of Annex no.2 of "Methodology for the calculation of core inflation index", approved by joint order of the National Bank of Moldova and National Bureau of Statistics N8-07-01203/6 of 19 January 2012 (the modification refers to the inclusion of prices for remote communication services and medicines in regulated prices).

Evolution of the NBM interest rates [1]

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