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## Mission of the National Bank of Moldova

*The National Bank of Moldova, as the central bank of the Republic of Moldova, is an autonomous public legal person, which establishes and promotes monetary and foreign exchange policy in the state, a fact stipulated in article 5 paragraph (1) letter a) of Law No. 548/1995 on the National Bank of Moldova.*

*Under the provisions of article 4 paragraph (1) of the Law No. 548/1995 on the National Bank of Moldova, the fundamental objective of the National Bank of Moldova is to ensure and maintain price stability. At the same time, article 4 paragraph (2) provides that, without prejudice to its fundamental objective, the National Bank shall aim to ensure the stability and viability of the banking system and support the general economic policy of the state.*

*The fundamental objective is achieved through the monetary policy framework associated with the direct inflation targeting regime.*

*The quantitative objective – the inflation target is to maintain inflation, as measured by the consumer price index, at 5.0% annually with a possible deviation of  $\pm 1.5$  percentage points.*

*In this regard, the National Bank of Moldova has a wide and well-defined range of instruments through which it promotes monetary policy and ensures the achievement of the inflation target. These include open market operations – the main monetary policy instrument, and the ancillary instruments are the standing facilities, the required reserve ratio and interventions on the domestic foreign exchange market.*

*At the same time, in order to achieving the inflation target, the National Bank of Moldova steers the conditions on the money market by setting by the Executive Board the main indicator for the short-term interbank money market – the base rate.*

*The exchange rate regime implemented by the National Bank of Moldova is that of managed floating and, respectively, the interventions on the domestic foreign exchange market are used only to support the effects of the implementation of open market operations, to the extent that they will be necessary to achieve the inflation target and without influencing the fundamental trends of the exchange rate of the national currency. At the same time, the NBM reserves the right to carry out foreign exchange interventions in order to mitigate excessive exchange rate fluctuations, to stop speculative operations and to replenish international foreign exchange reserves, without prejudice to the achievement of the inflation target.*

*The monetary policy decision regarding the base rate, the standing facility rates and the required reserve ratio is taken by the Executive Board of the NBM on the basis of the analysis of the latest information on the macroeconomic situation in the Republic of Moldova and the external economic environment, the trend of macroeconomic indicators in the medium-term, as well as the short- and medium-term inflation outlook, provided by the Monetary Policy Department of the NBM.*

*In this respect, the Executive Board of the NBM meets eight times a year in ordinary monetary policy meetings according to the approved schedule. Four monetary policy meetings are associated with the Inflation Report, while the other four meetings are devoted to the assessment of the deviation risks to the inflation forecast. At the same time, the Executive Board of the NBM reserves the right to meet in extraordinary meetings.*

## Introductory note

*The National Bank of Moldova appreciates the role of monetary policy transparency and predictability in strengthening institutional credibility and ensuring the inflation target.*

*In this context, the **Inflation Report** is the main communication tool reflecting the latest analysis of the situation in the internal and external environment, developments in the inflation process and economic activity, along with aspects related to the conduct of monetary policy.*

*At the same time, the Report incorporates the inflation forecast for the eight-quarter horizon and the risks and uncertainties associated with this projection.*

*The summaries of the minutes of the meetings of the Executive Board of the NBM regarding the promotion of the monetary policy are part of the Report and are published with a frequency of six months from the adoption of the decision in line with the Medium-term monetary policy strategy of the NBM (approved by the decision of the Council of Administration of the NBM no. 303 of December 27, 2012).*

*Statistical data have been taken from the National Bureau of Statistics, Ministry of Economic Development and Digitalization, Ministry of Finance, Eurostat, International Monetary Fund, National Agency for Energy Regulation, State Hydrometeorological Service.*

*Statistical information provided by international bodies, national statistical offices and central banks was also analyzed.*

*Some statistical data have been calculated by the National Bank of Moldova.*

*According to article 69 paragraph (2), the Inflation Report shall be submitted to the Parliament and the Government within 45 days after the end of the reporting quarter.*

*The Inflation Report, February 2024 was considered and approved for publication at the meeting of the Executive Board of the NBM on February 6, 2024.*

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*The Inflation Report, February 2024 is a translation of Raport asupra inflației, februarie 2024 in Romanian. In case of discrepancies, the version of **the Report** in the original language prevails.*

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## List of acronyms

<b>ANRE</b>	National Agency for Energy Regulation
<b>CHIBOR</b>	Average interest rate at which the contributors banks are available to lend funds in MDL to other banks, on the interbank monetary market
<b>CIS</b>	Commonwealth of Independent States
<b>CPI</b>	Consumer price index
<b>ECB</b>	European Central Bank
<b>ECF</b>	Extended Credit Facility
<b>EFF</b>	Extended Fund Facility
<b>EU</b>	European Union
<b>EUR</b>	Single European currency
<b>FAO</b>	Food and Agriculture Organization of the United Nations
<b>FCC</b>	Freely convertible currency
<b>FRS</b>	Federal Reserve System
<b>GDP</b>	Gross Domestic Product
<b>GVA</b>	Gross Value Added
<b>ICIS</b>	Independent Commodity Intelligence Services
<b>IMF</b>	International Monetary Fund
<b>JPY</b>	Japanese yen
<b>LB</b>	Local budgets
<b>LNG</b>	Liquefied Natural Gas
<b>MHIF</b>	Mandatory Health Insurance Fund
<b>MDL</b>	Moldovan leu
<b>MHIF</b>	Mandatory health insurance fund
<b>NBC</b>	Certificates issued by the National Bank of Moldova
<b>NBM</b>	National Bank of Moldova
<b>NBS</b>	National Bureau of Statistics of the Republic of Moldova
<b>NEER</b>	Nominal effective exchange rate of the national currency
<b>OPEC+</b>	The alliance between the Organization of the Petroleum Exporting Countries (OPEC) and a group of non-OPEC oil-producing countries.
<b>PMI</b>	Purchasing Manager's Index
<b>REER</b>	Real effective exchange rate of the national currency

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<b>RUB</b>	Russian ruble
<b>SB</b>	State budget
<b>SDR</b>	Special drawing rights
<b>SSIB</b>	State social insurance budget
<b>STA</b>	Single treasury account
<b>USD</b>	US Dollar

# Summary

## Inflation

*During 2023, the annual inflation rate continued the downward trend since the end of 2022, and in the last quarter it entered in the range of the inflation target. At the same time, in the fourth quarter of 2023, the annual inflation rate was lower than anticipated in the Inflation Report, November 2023. Thus, the annual inflation rate declined from 8.6% in September 2023 to 4.2% in December 2023. In October 2023, after a period of about two years, the annual inflation rate re-entered the range of  $\pm 1.5$  percentage points from the 5.0% target and remained within it until the end of the year. At the same time, the average annual inflation rate amounted to 5.3% in the fourth quarter of 2023, by 4.4 percentage points lower than in the previous quarter. The downward trajectory of inflation during the previous year and its placement within  $\pm 1.5$  percentage points of the 5.0% target in the fourth quarter of 2023 is largely the result of the restrictive monetary policy measures of the NBM initiated in the summer of 2021 and continued consistently until the end of 2022. These have succeeded in dampening the excessive aggregate demand in the post-pandemic period, which, together with other sectoral shocks, exerted pronounced inflationary pressures in that period. Subsequently, given the peculiarities of the transmission mechanism of the effects of monetary policy actions on the domestic economy, in the second half of 2022 and during 2023, as estimated, demand moderated and contributed, together with the decline in energy and food prices at the regional level, to the downward trajectory of the annual CPI rate. At the same time, this effect was also intensified by the exchange rate dynamics during 2023. At the same time, in November and December 2023 a temporary disinflationary impact was determined by the compensation of energy resources in the cold period of the year.*

*The downward trend in the annual rate of industrial production prices has continued, setting the stage for a moderation of their pressures on the prices of some CPI subcomponents in the period ahead. In addition, domestic demand will continue to exert a disinflationary impact, which will be mitigated by the adjustment of tariffs on some services and increases in excise duties on some CPI goods. The way in which tariffs are adjusted, as well as the tense situation in the region and the risks of its escalation, maintain a high degree of uncertainty regarding the inflation forecast, which is also intensified by the procedure for reflecting the compensation granted to the population during the cold period of the year.*

*In January 2024, the annual inflation rate remained within  $\pm 1.5$  percentage points of the inflation target of 5.0%, constituting 4.6%, by 0.4 percentage points higher than in December 2023. By subcomponents, the annual core inflation rate increased by 0.5 percentage points to 6.4%. The annual rate of prices of regulated goods and services amounted to 2.2%, by 2.1 percentage points higher than in December 2023. The annual rate of food and fuel prices decreased by 0.4 and 0.9 percentage points, respectively, to 4.2% and -2.3%, respectively.*

## External environment

*At the beginning of 2024, the world economy can be characterized by a certain stability overshadowed by many uncertainties and gloomy forecasts. Globally we have two major ongoing armed conflicts, the war in Ukraine and the conflict in Palestine. On top of these, attacks by Houthi rebels in Yemen on merchant ships in the Red Sea and counterattacks by the USA and allies have disrupted shipping through the Suez Canal, forcing traders to take a detour route around Africa, thus increasing logistics and transportation costs. Although inflation rates have come down towards the levels targeted by monetary authorities, they are in no hurry to cut interest rates because of persistent risks and uncertainties. These risks are related to the transportation costs, especially shipping, energy prices, the impact of El Niño on some agricultural crops and foreign exchange and financial risks. Economic growth continues to be weak under the burden of still high interest rates and structural shifts in global trade in recent years.*

### Economy

*In the third quarter of 2023, the annual GDP dynamics returned to the positive territory after the decline in the second half of 2022 and the first half of 2023. As a result, the GDP increased by 2.6% compared to the same period of 2022. This dynamic was marginally higher than that anticipated in the Inflation Report, November 2023. Developments in economic activity were mainly supported by the rich harvest in the agricultural sector, which created conditions for both higher exports and lower imports of agri-food products. There were also some positive developments in the financial sector, communications, social services, construction and real estate transactions. However, domestic demand continued to be modest, signaled by a decrease in the consumption of population and investment, amid weak real income growth and heightened uncertainty in the region. Less optimistic signals regarding the economic activity are also confirmed by negative dynamics in industry, trade and transportation, as well as a reduction in the net taxes on products. At the same time, the seasonally adjusted series reflects a 0.8% decline in GDP compared to the second quarter of 2023. Overall, in the first nine months of 2023, the GDP decreased by 0.4% compared to 2022. Against this backdrop, similar to the previous periods, as projected, the aggregate demand pressures on prices had exerted a disinflationary impact.*

*In the fourth quarter of 2023 as well, the GDP is expected to continue its positive dynamics on the basis of a rich harvest in the agricultural sector, an increase in exports overlapping with a subdued domestic demand affected by uncertainties in the region. Thus, according to the operational data published by the NBS for November 2023, exports and retail trade increased in nominal terms by 6.7% and 2.3%, respectively. Imports, industrial production, wholesale trade decreased by 14.7%, 6.1% and 3.5%, respectively. In terms of consumption financing sources, transfers to individuals declined by 12.8% annually.*

*In the fourth quarter of 2023, the national public budget revenue increased by 9.6% above the level recorded in the same period of 2022. National public budget expenditure increased by 8.7% above the level recorded in the fourth quarter of 2022. At the same time, on the market of state securities allocated during the fourth quarter of 2023, interest rates maintained their downward trend.*

### Monetary policy

*In the fourth quarter of 2023, the average excess liquidity amounted to MDL 9.4 billion, decreasing by MDL 0.6 billion compared to the previous quarter. In January 2024, excess liquidity averaged MDL 12.7 billion.*

*The M3 monetary aggregate in the fourth quarter of 2023 recorded an annual growth rate of 18.3% annually. The main contribution is provided by the deposits balance in national currency.*

*During the fourth quarter of 2023, two meetings of the Executive Board of the National Bank of Moldova were held on monetary policy decisions. Following the assessment of the balance of internal and external risks and the inflation outlook in the short- and medium-term, the Executive Board of the National Bank of Moldova, at its meeting on November 7, 2023, decided to lower the base rate applied to the main monetary policy operations by 1.25 percentage points to 4.75%, and subsequently, at its meeting on December 14, 2023, maintained this level.*

*At the same time, during the ordinary monetary policy meeting on February 6, 2024, the Executive Board of the National Bank of Moldova adopted unanimously the decrease of the base rate applied to the main short-term monetary policy operations by 0.50 percentage points, setting the level at 4.25%. Rates on overnight loans and deposits were lowered by the same magnitude, to 6.25% and 2.25%, respectively. At the same time, the required reserve ratio of funds attracted in MDL and non-convertible currency was maintained at the level of 33.0% of the calculation base. Meanwhile, the required reserve ratio from funds attracted in freely convertible foreign currency was maintained at the level of 43.0% of the calculation base.*

*This decision was taken in the context of a gradual adjustment of monetary policy so as to continue to stimulate credit and support domestic aggregate demand by encouraging consumption and investment, balancing the national economy and anchoring inflationary expectations, with the aim of keeping inflation within the variation range of the target over the medium-term.*

*Interest rates on new loans and deposits in national currency continued to decline in the fourth quarter of 2023, including as a result of cumulative monetary policy stimulative measures. Thus, the weighted average rate on loans amounted to 10.50% and that on deposits to 4.23%, decreasing by 3.64 and 9.0 percentage points, respectively, compared to the fourth quarter of 2022.*

*A similar downward trend was followed by the interest rates on the balances of loans and deposits in national currency. In this regard, the weighted average interest rate on the balance of loans in MDL decreased by 0.46 percentage points and amounted to 10.57% in the fourth quarter of 2023 compared to the fourth quarter of 2022. The weighted average interest rate on the balance of term deposits in MDL amounted to 7.24% annually, lower by 2.93 percentage points. Average interest rates on loans and deposits in foreign currency have maintained on an upward trend.*

## **Medium-term inflation projection**

*The current round of forecasting assumes that external demand will be weak relative to historical averages and that external inflation will trend towards the levels targeted by monetary authorities. Interest rates in the region and globally will decrease, but not as rapidly as previously anticipated. The US dollar will follow a slightly depreciating trend due to the low interest rates, renewed talks on raising the debt ceiling and the reduced attractiveness of the US dollar. The Russian ruble will fluctuate in the range of USD/RUB 90-100 according to the new foreign exchange reality, which is also the level desired/forecasted by the Russian authorities. Oil prices will be affected by the falling consumer demand in China and Europe as well as by the tensions in the Middle East. Natural gas prices will be stable and food prices on the international market will increase moderately compared to the previous years' peaks.*

*The annual inflation rate will have a relatively stable trend for the entire forecast period<sup>1</sup>. Inflation will slightly oscillate close to the 5.0% target and will remain within the variation range over the forecast horizon. The minimum value will be recorded in the second quarter of 2024 and in the second and third quarters of 2025, and the maximum value in the first quarter of 2025. The annual rate of core inflation will increase only slightly in the first half of this year, after which it will slightly decline until the end of the forecast horizon<sup>2</sup>, except in the last quarter of the forecast, when it will slightly increase. The annual rate of food prices will trend slightly downward for the early part of the forecast horizon, after which it will trend relatively steady until the end of the forecast period. The annual rate of regulated prices will decline in the first half of the current year, then will rapidly increase until the first quarter of 2025, then will decline in the following quarter and remain stable through the end of the forecast horizon. The annual rate of fuel prices is projected to slightly increase, at modest rates, until the end of the forecast horizon, with the exception of the third quarter of 2024.*

*Aggregate demand will be negative for the entire forecast period due to deteriorating external demand and modest financing of household consumption, as well as tightening monetary conditions. The rich agricultural harvest in the previous year and the positive fiscal impulse starting in the second quarter of 2025 for two consecutive quarters will mitigate the decline in aggregate demand.*

*Real monetary conditions are likely to be restrictive, albeit diminishing, on aggregate demand over the entire forecast period.*

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<sup>1</sup>First quarter of 2024 – fourth quarter of 2025

<sup>2</sup>Fourth quarter of 2025

*Current inflation forecast, compared to that in the previous inflation report<sup>3</sup>, has been revised downward insignificantly in the first quarter of 2024 and upward for the remainder of the comparable period<sup>4</sup>. The current forecast of the annual rate of core inflation has been revised significantly upward over the entire comparable period. The annual growth rate of food prices has been revised downward over the entire comparable period. The current forecast of the annual rate of regulated prices is revised significantly upwards over the entire comparable period, except for the first quarter of 2024. The forecast for the annual rate of fuel prices has been lowered for the entire comparable period.*

*Risks and uncertainties associated with the current forecast remain high. The identified proinflationary risks from the external environment are the tensions in the Middle East, the prolonged blockage of access to transportation across the Red Sea, the war in Ukraine, rising consumer prices in Türkiye and the Russian Federation, and possible temporary supply shocks to international food price formation. Currently, a disinflationary risk is the continued sharp moderation in the rate of economic activity in the eurozone. Uncertainties relate to the transition period from tighter monetary conditions to lower interest rates in the region and globally and the geopolitical configuration after the 2024 electoral elections. Among the main domestic uncertainties are the timing and magnitude of the adjustment of tariffs for regulated services, changes in the CPI basket weights, the way the energy compensations to the population during the cold period of the year is reflected in the statistics, external financing, refugee inflows, weather conditions and the upcoming harvest.*

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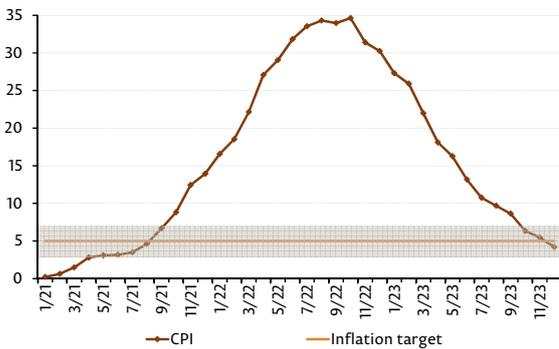
<sup>3</sup>Inflation Report, November 2023

<sup>4</sup>First quarter of 2024 – third quarter of 2025

# Chapter 1

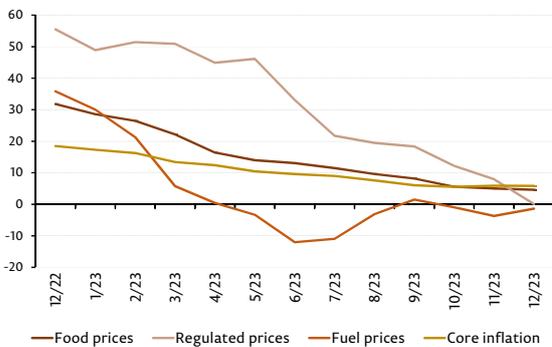
## Inflation evolution

Chart 1.1: Annual CPI rate (%)



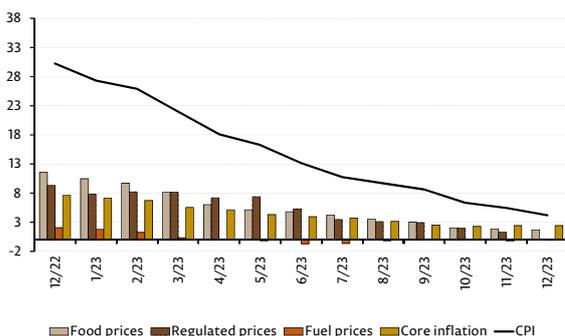
Source: NBS, NBM

Chart 1.2: Annual rate of the main CPI subcomponents (%)



Source: NBS

Chart 1.3: Annual inflation evolution (%) and contribution of subcomponents (percentage points)



Source: NBS, NBM calculations

### 1.1 Consumer price index

**Over the course of 2023, the annual inflation rate continued the downward trend since the end of 2022, and in the last quarter it entered the inflation target range. At the same time, in the fourth quarter of 2023, the annual inflation rate was lower than anticipated in the Inflation Report, November 2023.**

The annual inflation rate decreased from 8.6% in September 2023 to 4.2% in December 2023. In October 2023, after a period of about two years, the annual inflation rate re-entered of the  $\pm 1.5$  percentage points range of 5.0% inflation target and remained within this range until the end of the year. At the same time, the average annual inflation rate was 5.3% in the fourth quarter of 2023, 4.4 percentage points lower than in the previous quarter.

The downward trajectory of inflation over the previous year and its placement in the range of the  $\pm 1.5$  percentage points of 5.0% inflation target in the fourth quarter of 2023 is also largely the result of the restrictive monetary policy measures of the NBM initiated in the summer of 2021 and consistently applied until the end of 2022. They were successful in dampening excessive aggregate demand in the post-pandemic period and which, together with other sectoral shocks, exerted pronounced inflationary pressures in that period. Accordingly, subsequently, given the peculiarities of the transmission mechanism of the effects of monetary policy actions on the domestic economy, in the second half of 2022 and during 2023, as estimated, demand moderated and contributed, together with the decline in regional energy and food prices, to the downward trajectory of the annual rate of CPI. At the same time, this effect was also accentuated by the exchange rate dynamics during 2023. At the same time, in November and December 2023 a temporary disinflationary impact was induced by the compensation of the population for energy resources during the cold period of the year. However, although declining, core inflation and food prices continued to make positive contributions during the fourth quarter of 2023. These were largely driven by cost pressures, which gradually eased, and some adverse sectoral developments.

The annual dynamics of the CPI in the fourth quarter of 2023 was lower than the figure anticipated in the Inflation Report, November 2023 as a result of the unanticipated decrease in the tariff for electricity supplied by "Premier Energy" and "FEE-North" in mid-November, as well as the impact of reflecting the compensation to the population for energy resources during the cold period of

the year. At the same time, a smaller negative deviation was recorded for the forecast of food prices in the context of seasonal fluctuations, but also the effect of favorable weather conditions for some agricultural crops. A negative deviation was also recorded for the fuel price forecast, against the background of a lower trajectory for oil prices, but its impact on the total deviation was less pronounced. In the period ahead, the annual rate of CPI will remain within the inflation target range.

In January 2024<sup>5</sup>, the annual inflation rate remained within the range of  $\pm 1.5$  percentage points from the inflation target of 5.0%, constituting 4.6% and being 0.4 percentage points higher than that of December 2023.

## Core inflation

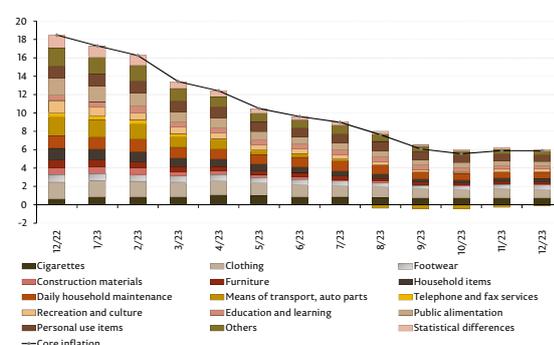
**The annual core inflation rate continued the downward trajectory initiated at the end of 2022, averaging 5.8% in the fourth quarter of 2023, or 1.8 percentage points lower than in the previous quarter.**

The gradual moderation in the annual rate of core inflation during 2023 can be associated with the gradual dissipation of second-round effects associated with the adjustments in tariffs for mains gas, electricity, and fuel from the previous year. At the same time, the moderation in core inflation can also be attributed to more modest demand. In this regard, similar to previous periods, aggregate demand continued to exert disinflationary pressures on the components of core inflation in the fourth quarter of 2023, against the background of modest growth in real disposable income of the population. At the same time, disinflationary pressures on core inflation in this period were also exerted by exchange rate dynamics. Cost pressures are estimated to have gradually lost some of their intensity. At the same time, there has been a slight increase in the annual core inflation rate over the past two months, largely in the context of adverse sectoral developments. Thus, it increased from 5.6% in October 2023 to 5.9% in December 2023.

In structure, the moderation in the annual core inflation rate was mainly supported by the decreasing impact of the subcomponents "daily household maintenance", "clothing", "public alimentation", "personal use items", "education and learning", "furniture", "means of transport, auto parts", in the context of the influence of the above-mentioned factors (Chart 1.4).

In December 2023, within the annual dynamics of core inflation (5.9%), the most pronounced increases in annual terms were recorded in the subcomponents "cigarettes" (17.4%), "education and learning" (14.3%), "daily household maintenance" (11.4%), "personal use items" (10.0%), "footwear" (9.6%), "public alimentation" (6.5%) and "clothing" (5.9%).

Chart 1.4: Contribution of subcomponents (percentage points) to annual core inflation dynamics (%)



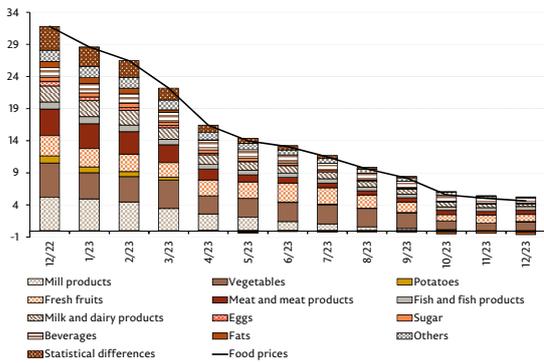
Source: NBS, NBM calculations

<sup>5</sup>In accordance with the Methodology for calculating the Consumer Price Index, expenditure weights are estimated by applying the geometric mean of the household's monetary expenditures according to the Household Budget Survey (HBS) and the data on final consumption of households at COICOP class level from the National Accounts for the year "t-2" (with some exceptions, mentioned in the nominated methodology). Thus, starting from January 2024, CPI calculations are made using weighting coefficients calculated on the basis of data for 2022.

The subsequent trend in the prices of important categories of goods included in core inflation, in the absence of supply-side imbalances, will continue to reflect the effect of still modest domestic demand.

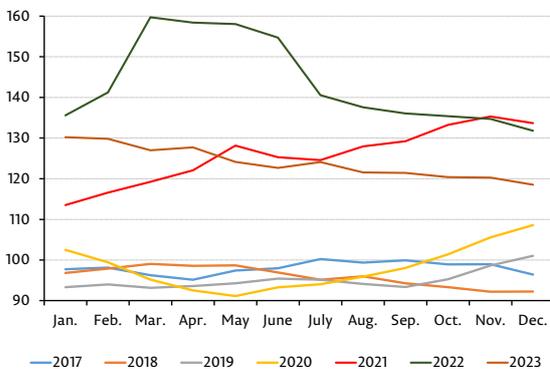
In January 2024, the annual core inflation rate reached 6.4%, 0.5 percentage points higher than in December 2023.

Chart 1.5: Contribution of components (percentage points) to annual food prices dynamics (%)



Source: NBS, NBM calculations

Chart 1.6: Evolution of the international food price index, FAO index



Source: FAO, NBM calculations

### Food prices

**In the fourth quarter of 2023, the annual rate of food prices continued the downward trend that started in the autumn of 2022.**

Thus, in the fourth quarter of 2023, it registered an average rate of 5.1% or 4.7 percentage points lower than in the third quarter of 2023. Similar to previous periods, the "vegetables", "fresh fruits", "meat and meat products" and "beverages" groups contributed the most to the formation of the annual rate of food prices, but their contribution is continuously decreasing (Chart 1.5).

It should be noted that during the fourth quarter of 2023 there was a lull in food prices. Thus, the lack of inflationary pressures on the international market, the shortage of demand on the domestic market, the rich agricultural year, the lack of pressures from the MDL/USD exchange rate, overlapping with the decrease in cost pressures contributed to the moderation of the growth rates of food prices during the analyzed period.

At the same time, the level of food prices on the international market is continuously falling (Chart 1.6). They have thus exerted disinflationary pressures on domestic prices. In the fourth quarter of 2023, the annual rate of food prices on the international market amounted to -10.6%.

Over this period, the contribution from food prices to the formation of the annual inflation rate decreased by 1.7 percentage points, to the level of 1.9 percentage points.

In January 2024, the annual growth rate of food prices constituted 4.2%, 0.4 percentage points lower than in December 2023.

### Regulated prices

**In the fourth quarter of 2023, the annual rate of regulated prices continued the downward trajectory of previous periods. These dynamics were determined, on the one hand, by the decrease in some tariffs during the fourth quarter of 2023 and, on the other hand, by the effects of the compensations on energy resources granted to the population for the period November 2023 – March 2024, which supported the fall in final prices for consumers of mains gas, central heating, electricity (Chart 1.7).**

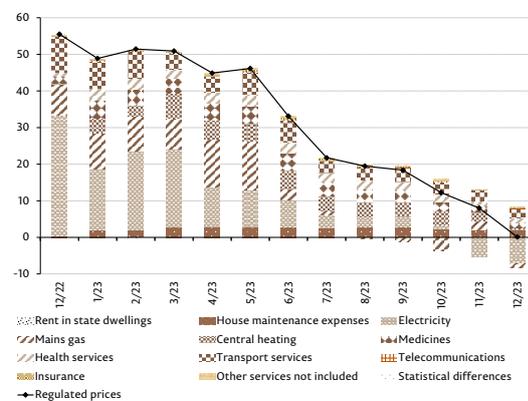
The annual rate of regulated prices was 0.1% in December 2023, 18.3 percentage points lower than in September 2023. The average annual rate of regulated prices in the fourth quarter of 2023 was 6.8%, 13.1 percentage points lower than in the third quarter of 2023.

With the beginning of the cold season, in November 2023 the state program on compensation of energy resources for the population for the period from November 2023 – March 2024<sup>6</sup> started. As a result, the subcomponents with a major share in the regulated prices were affected by this program in the sense of lowering the CPI prices for central heating, mains gas and electricity<sup>7</sup>. However, the decrease in the tariff for the "electricity" subcomponent (-4.7% in November and -3.9% in December) is largely due to the decrease in the tariff by ANRE decision, but it also contains the effect from the mentioned compensations. In this regard, on November 10, the electricity tariffs were adjusted<sup>8</sup> (effective from November 14, 2023<sup>9</sup>). Thus, for "Premier Energy" consumers in the center and south of the country, a tariff has been set in the amount of 2.39 bani/kWh – low voltage (0.4 kV), 18 bani/kWh less than the previous price, and for "FEE-Nord" consumers in the north of the country, a tariff of 2.88 bani/kWh – low voltage (0.4 kV), 32 bani/kWh less than the previous price.

As a result of the examination and approval of the draft decision on the tariffs for regular transport services, in electric transport, starting October 1, the charge for a trip in the city of Balti is MDL 4, one MDL less than the previous tariff<sup>10</sup>. In this way, prices for urban transportation services in the CPI decreased by 1.3%. At the same time, in the context of the decrease in fuel prices in recent months, the prices of intercity transportation services decreased by 2.3% during the fourth quarter of 2023 according to the methodology for setting the respective tariffs. In contrast, prices for air transportation services during the quarter increased by 6.3%.

In mid-October, ANRE approved lower tariffs for household consumers for the supply and provision of public water supply service by S.A. "Apa-Canal Chisinau"<sup>11</sup>. Following the analysis of

Chart 1.7: Evolution of regulated prices (%) and contribution subcomponents (percentage points)



Source: NBS, NBM calculations

<sup>6</sup>[https://cancelaria.gov.md/sites/default/files/document/attachments/nu-876-mmps-2023\\_0.pdf](https://cancelaria.gov.md/sites/default/files/document/attachments/nu-876-mmps-2023_0.pdf)

<sup>7</sup>In accordance with the Methodology for calculating the Consumer Price Index, when estimating the effective average prices/tariffs for the supply of mains gas, electricity and central heating, the NBS took into account the compensations granted by the Government for the payment of energy bills for household consumers, in compliance with the Law No. 241/2022 on the Energy Vulnerability Reduction Fund, as well as Government Decisions No. 704/2022 and No. 814/2022. The preliminary estimate of the effective average price of energy resources in November this year (taking into account the compensations in the invoice) was made on the basis of the information available at the time of establishing the CPI calculations. When preparing the CPI data in the coming months, new available data on the supply of energy resources (including possible recalculations made in the invoice by operators/suppliers) will be taken into account – *taken from the official NBS website*.

<sup>8</sup><https://anre.md/anre-a-micsorat-preturile-reglementate-pentru-furnizarea-energiei-electrice-3-777>

<sup>9</sup>Monitorul oficial No. 426-429 of 14.11.2023, p. 91-92

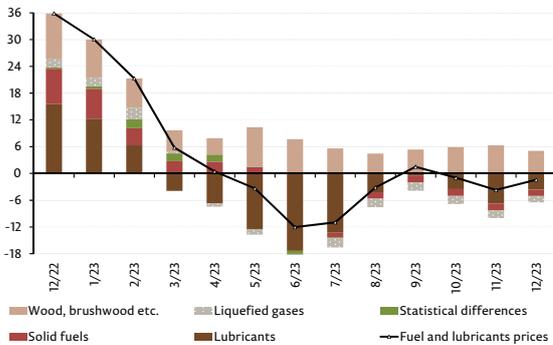
<sup>10</sup><https://tvn.md/se-ieftinesc-calatoriile-cu-troleibuzul-la-balti-cat-vor-costa-din-octombrie/>

<sup>11</sup><https://www.anre.md/consumatorii-din-municipiul-chisinau-vor-plati-mai-putin-pentru-serviciul-de-apa-si-de-canalizare-3-762>

the application submitted by the operator and according to the analysis of the determined values, a new tariff for the provision of public water supply service to all consumers was approved in the amount of MDL 10.79/cubic metre, MDL 0.33/cubic metre lower than the previous one. In the case of the public sewerage and wastewater treatment service for household consumers, the current tariff remained unchanged at MDL 4.18/cubic metre (in force from October 12<sup>12</sup>). As a result, the water supply and sewerage component decreased by 1.0% at the country level. Also, on December 12, 2023, was adjusted the water and sewerage tariff in the Edinet city. Thus, the tariff for the public drinking water supply service for households was set at MDL 32.31/cubic metre (MDL +12.61/cubic metre compared to the previous tariff), and for the public sewerage and wastewater treatment service for households – at MDL 10.15/cubic metre (MDL +5.15/cubic metre compared to the old tariff)<sup>13</sup>. Thus, at the country level, this adjustment produced a 2.8% price increase for the water supply and sewerage component in December 2023. The rest of the impact is to be reflected by the NBS in January 2024. At the same time, during the fourth quarter of 2023, a positive impact in regulated prices was driven by the increase in medicines prices, which cumulatively increased by 1.8%.

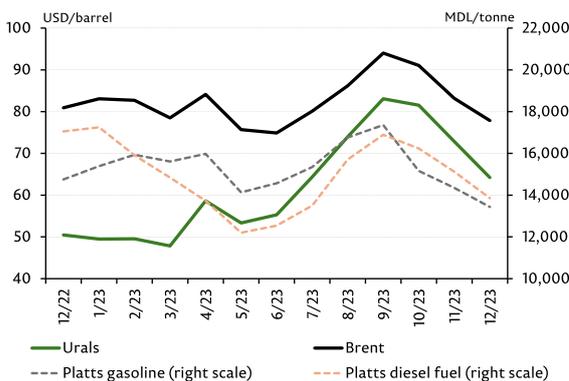
In January 2024, the annual rate of prices of regulated goods and services amounted to 2.2%, 2.1 percentage points higher than in December 2023.

Chart 1.8: Contribution of components (percentage points) to the annual increase in fuel and lubricants prices (%)



Source: NBS, NBM calculations

Chart 1.9: Evolution of average Platts quotations, Urals oil and Brent oil prices



Source: ANRE, NBM calculations

### Fuel and lubricants prices

**The annual rate of fuel and lubricants prices returned to negative territory in the fourth quarter of 2023, amid lower oil prices between October and December 2023.**

Thus, the annual rate of fuel and lubricants prices decreased from 1.5% in September 2023 to -1.4% in December 2023 under the influence of the decrease in the prices of "lubricants". This development was mainly driven by the decrease in "lubricants" prices as a result of the decrease in gasoline and diesel prices carried out by PECO stations during the quarter. These decreases were dictated by the average Platts quotations for gasoline and diesel fuel, which averaged around MDL 14,315.6/tonne and MDL 15,064.1/tonne in the quarter under reference, respectively, decreasing by 13.2 and 2.0% compared to the third quarter of 2023 (Chart 1.9). The decrease in the above-mentioned quotations was generated by the downward trend in the price of Brent crude oil, by 3.1% compared to the previous quarter. The annual average rate of fuel and lubricants prices in the fourth quarter of 2023 amounted to -2.0%, 2.2 percentage points higher than in the third quarter of 2023 (Chart 1.8).

During the fourth quarter of 2023, the prices of "wood, brushwood etc." continued to exert a positive impact, while the prices of "solid fuels" and "liquefied gases" had a negative impact on the annual rate of fuel and lubricants prices.

In January 2024, the annual rate of fuel and lubricants prices amounted to -2.3%, which is 0.9 percentage points lower than in December 2023.

<sup>12</sup>Monitorul oficial No. 383-386 (8889-8892) of 12.10.2023

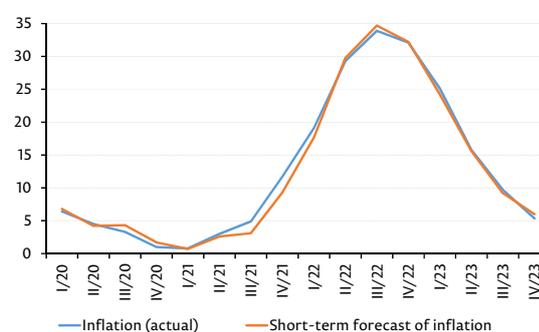
<sup>13</sup>Monitorul oficial No. 477-479a (8983-8985a), p. 14

## 1.2 Inflation evolution and short-term forecast assessment from the Inflation Report, November 2023

***In the forecasting round of the Inflation Report, November 2023, the annual CPI rate was expected to continue to decline to a level of 5.7% in December 2023 and recording an average value of 6.0% in the fourth quarter of 2023<sup>14</sup>. Inflation data for the fourth quarter of 2023 point to a lower trajectory than anticipated in the previous round of forecasts (Inflation Report, November 2023).***

In the fourth quarter of 2023, the annual inflation rate amounted to 5.3% and was 0.7 percentage points lower than anticipated in the forecast (Table 1.1). This was mainly due to the negative deviation recorded for the forecast of regulated and food prices and, to a lesser extent, for the forecast of fuel and lubricants prices. In this regard, in the fourth quarter of 2023, the annual rate of regulated prices amounted to 6.8% in the fourth quarter of 2023, 4.2 percentage points lower than expected, which is due to the unanticipated decrease in the Inflation Report, November 2023 of the electricity tariff supplied by "Premier Energy" and "FEE-Nord" in mid-November 2023, as well as the impact of the reflection of compensation to the population for energy resources in the cold period of the year. At the same time, the annual rate of food prices recorded the value of 5.1%, 1.1 percentage points lower than expected, which may indicate possible fluctuations in the seasonal effect, as well as the effect of favorable weather conditions for some agricultural crops. A negative deviation was also recorded for the fuel and lubricants price forecast, but its impact on the total deviation was less pronounced. In this respect, the annual rate of fuel and lubricants prices was -2.0%, 1.8 percentage points lower than expected due to a lower trajectory of oil prices. At the same time, the impact of the negative deviations in the subcomponents mentioned above was partly offset by a stronger increase in core inflation. In this regard, in the fourth quarter of 2023, the annual rate of core inflation amounted to 5.8%, 1.3 percentage points higher than expected.

Chart 1.10: Annual rate of CPI (%)



Source: NBS, NBM

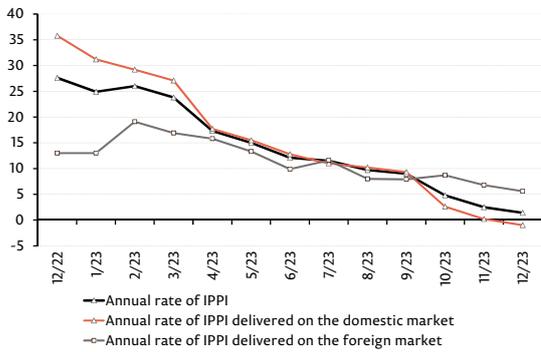
Table 1.1: The evolution and forecast of CPI and its components

	De facto Q IV, 2023/ Q IV, 2022 (%)	Forecast* Q IV, 2023/ Q IV, 2022 (%)	Deviation (De facto- forecast) (p.p.)
<b>CPI</b>	<b>5.3</b>	<b>6.0</b>	<b>-0.7</b>
Core inflation	5.8	4.5	1.3
Food prices	5.1	6.2	-1.1
Regulated prices	6.8	11.0	-4.2
Fuel prices	-2.0	-0.2	-1.8

Source: NBS, NBM calculations  
\*Forecast from Inflation Report, November 2023

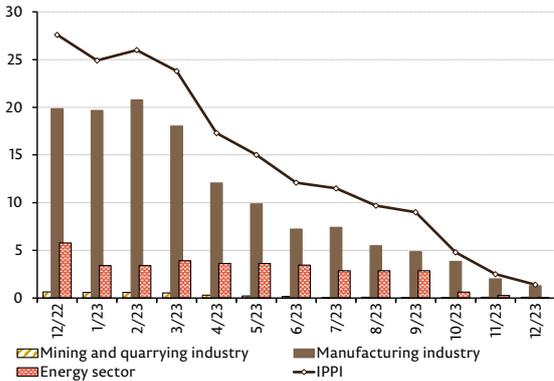
<sup>14</sup>In view of the more pronounced volatility of the monthly values, as well as some possible measurement errors, which should normally not influence monetary policy decisions, the short-term inflation forecast is carried out on a quarterly basis. This value is an input into the medium-term inflation projection, which is similarly quarterly and underpins monetary policy decisions. At the same time, it is reported in the Inflation Reports. However, the actual monthly CPI data, as they are published by the NBS during the quarter, are analyzed and compared with the short-term forecast for the whole quarter to assess whether the main assumptions are confirmed or whether there is a risk of marked deviations from the forecast. Therefore, deviations between the actual data available for the months within the quarter and the short-term inflation forecast need to be interpreted appropriately, also taking into account the assumptions/ expectations for the remaining months of the quarter.

Chart 1.11: Annual industrial price rate (%)



Source: NBS

Chart 1.12: Annual industrial price rate (%) and its components contribution classified by main branches (percentage points)



Source: NBS, NBM calculations

### 1.3 Industrial production prices

**In the fourth quarter of 2023, the annual industrial price rate averaged 2.9%, or 7.2 percentage points lower than in the third quarter of 2023.**

In terms of structure, both the annual rate of prices of products delivered on the domestic market and the annual rate of prices of products delivered on the foreign market followed a downward trend (Chart 1.11).

Analyzing the evolution of the annual industrial price index by main branches, it can be seen that its marked moderation was supported by the dynamics in the manufacturing industry and the energy sector (Chart 1.12). Thus, the annual price rate in manufacturing industry averaged 2.6% or 3.9 percentage points lower than in the previous quarter. The sharp decrease in the contributions from "food industry" and "other non-metallic mineral products" mainly contributed to the downward trend in the annual rate of prices in the manufacturing industry. It should be noted that during the analyzed period the annual price rate in the energy sector was 4.5% or 39.4 percentage points lower than in the third quarter of 2023. In the fourth quarter of 2023, prices in the mining and quarrying industry increased in annual terms by 3.5%, generating a minor contribution to the total price dynamics in the industry.

## Chapter 2

### External environment

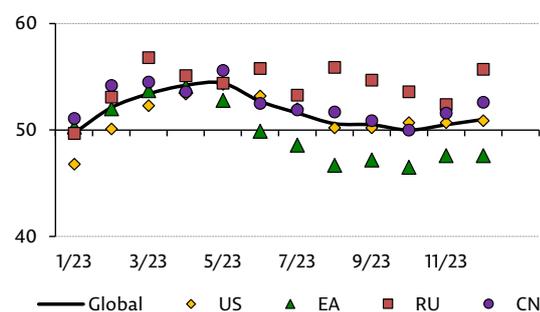
*At the beginning of 2024, the world economy can be characterized by a certain stability overshadowed by many uncertainties and gloomy forecasts. Globally we have two major ongoing armed conflicts, the war in Ukraine and the conflict in Palestine. On top of these, attacks by Houthi rebels in Yemen on merchant ships in the Red Sea and counter-attacks by the US and allies have disrupted shipping through the Suez Canal, forcing traders to take a detour route around Africa, thus increasing logistics and transportation costs. Although inflation rates have come down towards the levels targeted by monetary authorities, they are in no hurry to cut interest rates because of persistent risks and uncertainties. These risks are related to transportation costs, especially shipping, energy prices, the impact of El Niño phenomenon on some agricultural crops, and currency and financial risks. Economic growth continues to be weak under the burden of still-high interest rates and structural shifts in global trade in the recent years.*

#### 2.1 World economy, financial and commodities markets

**PMI indexes** reflect a weak global economic growth. The US economy is apparently doing better than other economies, which has allowed the Federal Reserve System (FRS) to intervene more aggressively in the money market and, most likely, is under no pressure to cut interest rates at a rapid pace. The situation is more precarious in the euro area economy, where economic growth is weak and largely due to the slowdown in the industrial sector. Germany's GDP fell by 0.3% in 2023, according to new data from the country's Federal Statistical Office, after growing by 1.8% in 2022. Although China's GDP grew by 5.2% in 2023 and reached the level targeted by the authorities, it still faces significant challenges from deflationary pressures and the real estate crisis, and investors are not enthusiastic about policies aimed at maintaining the economic impulse. The Russian Federation's economy continues to benefit fully from relatively high oil prices, appropriate monetary policy measures and the ability to bypass the economic sanctions (Chart 2.1).

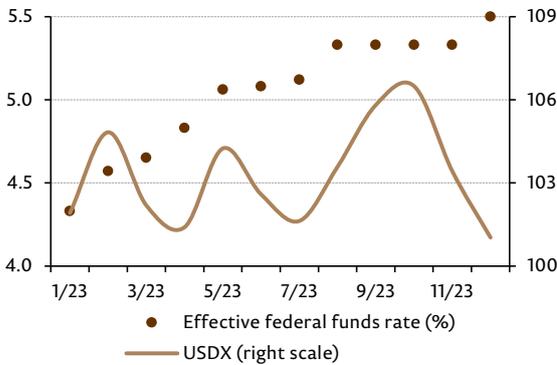
In the last few months of 2023, the **US dollar** depreciated against other international currencies due to expectations of interest rate cuts by the FRS. At recent monetary policy meetings, the FRS has maintained the range of interest rates at 5.25-5.5% (Chart 2.2). In November 2023, the US annual inflation rate fell to 3.1%, after which it rose again to 3.4% in December 2023. This has lowered some of the market's expectations of a rapid decline in interest rates by the FRS, especially as the US economy is performing relatively well and there is not yet a pressing need for monetary stimulus.

Chart 2.1: Development of the PMI indexes



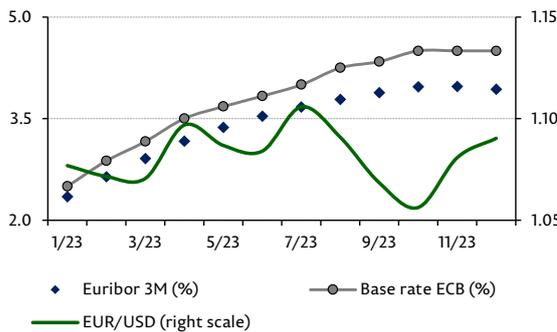
Source: Markit

Chart 2.2: Development of the USD index (DXY\*) in the context of the FRS's monetary policy



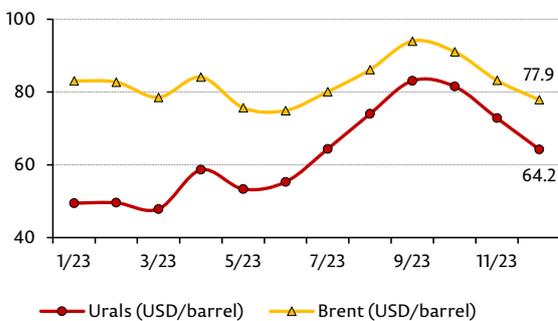
Source: FRS, Bloomberg  
 \*DXY is an index calculated by the weighted geometric average of the value of the US dollar against a basket of foreign currencies: euro – 57.6%, Japanese yen – 13.6%, British pound – 11.9%, Canadian dollar – 9.1%, Swedish krona – 4.2%, Swiss franc – 3.6%

Chart 2.3: Development of EUR/USD (monthly average) and interest rates in the euro area



Source: ECB

Chart 2.4: Development of oil quotations (USD/barrel)



Source: World Bank, Ministry of Finance of the Russian Federation

**The single European currency** followed an appreciating trend against the US dollar in the last months of 2023, surpassing the EUR/USD 1.11 parity at the end of December 2023. Christine Lagarde, president of the European Central Bank, said that while pro-inflationary pressures are expected to ease further, headline inflation could rise slightly again in the coming months, mainly due to some base effects. The ECB chief added that wage pressures remain strong and have become a key driver of domestic inflation. Euro area inflation fell by much more than expected, to 2.4% in November 2023 (the lowest annual pace since July 2021), but rose to 2.9% in December 2023. At the last two monetary policy meetings, the ECB has maintained the base rate at 4.5% (Chart 2.3).

After breaching the USD/RUB 100 level in early October 2023, **the Russian ruble** gradually appreciated to the USD/RUB 90 level where it stabilized. The Russian ruble strengthened on the background of an improving trade balance as well as a rise in the base rate. The appreciation of the Russian ruble was also supported by the rapid increase in the Bank of Russia's monetary policy rate from 7.5% in July 2023 to 16.0% in December 2023. The forecast of the Ministry of Economic Development of the Russian Federation, used in the budget calculation, assumes an average exchange rate of USD/RUB 90.1 in 2024, which is broadly in line with market expectations. The ruble depreciated slightly against the euro on New Year's Eve, when Russians usually buy foreign currency for trips abroad.

**Oil quotations** had on average declined slightly over the final months of 2023 (Chart 2.4). The OPEC+ decision to cut oil production and tensions in the Middle East created expectations of higher oil prices, but this did not materialize. Downside risks to global demand have once again come to the fore amid slowing economies in Europe and China. Weakness of European economies are putting pressure on the industrial sector in the region and causing a fall in demand for oil products. In China, state-owned refineries have cut oil refining volumes due to falling margins. Oil prices also fell sharply after the postponement of the OPEC+ meeting due to disputes over production quotas. The meeting, however, took place on December 1, 2023 and OPEC+ agreed to cut oil production by about 2 million barrels per day. Saudi Arabia will extend production cuts by more than 1 million barrels per day and Russia will cut production by 500,000 barrels per day. As of December 2023, the price of Brent brand oil has risen slightly again, above USD 80/barrel, due to tensions in the Red Sea and the halt in production at Libya's El Sharara oil field due to protests. Geopolitical tensions further escalated in the Middle East when, in early January 2024, the United States and allies retaliated against Houthi rebels in Yemen for attacks on ships in the Red Sea. However, oil prices continued to fall in early 2024 as traders' optimism about lower interest rates faded and Saudi Arabia cut its official selling price for exports in February. India also halted its USD 600 million program to replenish strategic oil reserves. The prospect of surplus supply, an uncertain economic outlook and a lack of clarity on how the situation in the Middle East will unfold are prompting analysts to avoid making forecasts.

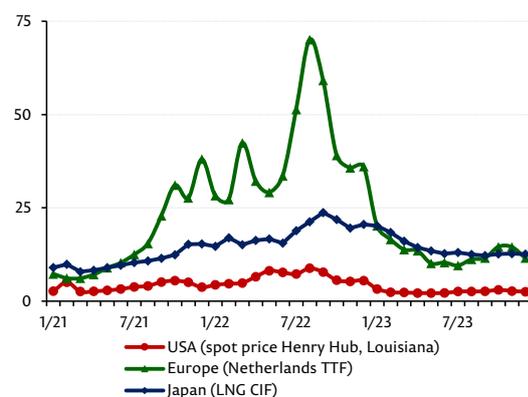
**European natural gas prices** rose slightly at the beginning of the fourth quarter of 2023 due to increased demand at the start of the cold season in the northern hemisphere and under

the conditions in which a leak in a pipeline was certified in the Baltic region. Also, Australian LNG workers went on strike and negotiations with Chevron were stalled. Another factor was the tensions in the Middle East, which prompted Israel to halt the exploitation of a major gas field in the Mediterranean Sea. Towards the end of 2023, however, European natural gas prices resumed their downward trend as milder weather in North Asia and Europe reduced the need to buy more fuel for the winter. Even though temperatures dropped significantly in Europe at the end of January 2024, traders are confident that Europe's ample supplies will be enough to get through the winter. However, natural gas prices in Europe remain high compared to pre-war price levels in Ukraine, while demand from large consumers such as industrial producers is falling, slowing economic growth. Industrial gas demand in 12 European countries, including the UK, was 23.5% below the 2017-2021 period average, according to ICIS<sup>15</sup> (Chart 2.5).

Since the beginning of 2023, **international market price indexes** calculated by the World Bank have recorded negative annual growth rates as a result of the high base in 2022. Tighter monetary conditions have also moderated global demand. The data for December 2023 reveals that the biggest decrease was in **fertilizer prices** which fell by 36.0% compared to the same period last year, followed by **energy resource prices** by 24.0%, **metals and minerals prices** by 4.9% and **agricultural products prices** by 2.4% (Chart 2.6). It should be noted that the risks associated with the increase in raw material prices in 2024 will be determined by the evolution of the consumer demand, the consequences of geopolitical tensions, logistics and transportation costs and the El Niño effect on some agricultural crops.

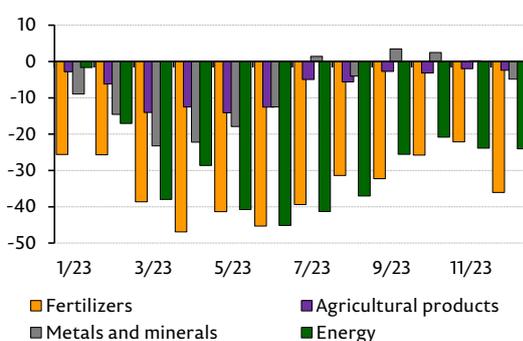
**International food prices** continued to decline in annual terms, but at slower rates compared to the first half of 2023. Thus, in December 2023, the FAO index recorded a 10.1% annual decline, of which the "cereals" group decreased by 16.6%, dairy by 16.0%, oils by 15.3%, meat by 1.8%, and sugar rose by 14.9% (Chart 2.7). After declining for four consecutive months, wheat export prices rose in monthly terms in December 2023, supported by agrometeorological-related logistical disruptions at some major exporters and tensions in the Black Sea amid robust demand. Corn prices on the world market also rose on concerns about the harvest in Brazil and logistical constraints hampering shipments from Ukraine. Rice prices on the international market have recorded an annual growth of about 21% in 2023, largely due to concerns about the impact of El Niño on rice production and as a result of export restrictions imposed by India. Oilseed prices have declined on the back of robust supply and low demand. Against the backdrop of increased demand during the holiday season, dairy prices rose slightly, especially in Europe, while meat prices fell due to very low demand in Asia.

Chart 2.5: International natural gas prices (USD/MMbtu)



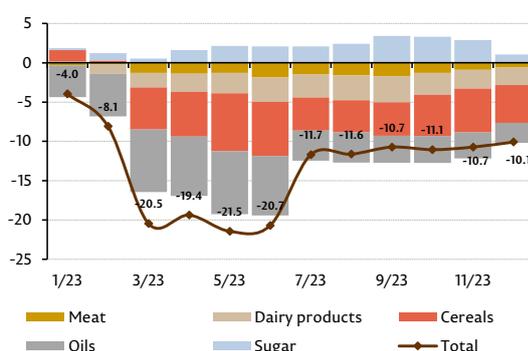
Source: World Bank

Chart 2.6: Annual growth rate of world price indexes (%)



Source: World Bank, NBM calculations

Chart 2.7: Annual growth rate of world food prices (FAO index)(%)



Source: FAO, NBM calculations

<sup>15</sup>Independent Commodity Intelligence Services

## 2.2 Evolution of important economies

In the third quarter of 2023, the gross domestic product of the **United States of America** increased by 1.2% compared with the previous quarter and 2.9% compared to the same period last year (in seasonally adjusted terms). In 2023, industrial production in the US increased by only 0.1% compared with 2022, and in December 2023 the US registered unemployment rate was 3.7%. In December 2023, consumer prices fell by 0.1% compared to November 2023, but were 3.4% higher than in December 2022.

The economy of **United Kingdom** has performed better than expected in 2023. Economists forecast an increase of 0.5% compared to a decrease of 1.0% at the start of 2023. In the third quarter of 2023, business investments increased by 6.3%, and household consumption – the main driver of growth in normal times – increased by 0.3%, but is still well below the pre-pandemic level, largely because of successive shocks to real incomes. Headline inflation fell to 3.9% in December 2023 on the background of lower energy prices.

Over the reference period, the economic activity in the **euro area** shrank marginally, by 0.1%, compared to the previous quarter, and compared to the same quarter in 2022, the euro area economy shrank by 0.3%. In the first 11 months of 2023, industrial production in the euro area contracted by 2.8% and the unemployment rate has remained at a minimum level of 6.4% in recent months. Consumer prices rose more moderately, in December 2023 harmonized annual inflation recorded a positive monthly rate of 0.2%, and on an annual basis an increase of 2.9%.

The GDP of **Germany** fell by 0.3% in 2023, according to new data from the country's Federal Statistical Office, after an increase of 1.8% in 2022. However, Germany's economy was 0.3% larger in 2023 than in 2019, the year before the pandemic. In January-November 2023, Germany's industrial production contracted compared with the same period in 2022 by 1.5% on a seasonally adjusted basis, due to higher energy costs and weaker domestic and foreign demand. Reflecting the impact of higher energy bills and higher borrowing costs on consumers, household consumption fell by 2.01% compared to the previous year, while government spending declined 1.6%. In addition to having one of the worst performances among advanced economies last year, it is also expected to record the worst performance in 2024. EU forecasts published in November show a growth of just 0.8%. Experts say that the country's economy is in a permanent "crisis mode" as supply chain problems, persistent inflationary pressures, weaker global demand for manufactured goods and higher interest rates have impacted domestic production.

In the third quarter of 2023, the gross domestic product of **France** fell by 0.1% (in seasonally adjusted terms) compared with the previous quarter, and compared with the same period of 2022, on a gross series basis it increased by only 0.3%. In January-November 2023, France's industrial production increased insignificantly compared with the same period of 2022, by 0.7% on the gross series. France's central bank has slightly lowered its

growth forecast for the country's economy to 0.8% for 2023, but expects a gradual increase thereafter through 2026 as inflation continues to fall.

In the third quarter of 2023, the gross domestic product of **Italy** stagnated both compared to the previous quarter and compared to the same period of 2022. In January-November 2023, Italy's industrial production contracted compared with the same period of 2022 by 2.6% on a seasonally adjusted basis. According to the National Statistical Institute, Italy's GDP will grow by 0.7% in both 2023 and 2024, slowing compared to 2022. Domestic demand will be mainly driven by private consumption, due to a slowdown in inflation, coupled with a gradual (albeit partial) recovery in wage and employment growth. Investments, although still growing, will decline significantly compared to 2022 and 2023 (+0.6% in 2023 and 2024). The deceleration in inflation, mainly driven by the fall in energy raw materials prices and the restrictive monetary policies implemented by the ECB, will moderate the growth rate of the deflator of resident household expenditure.

The gross domestic product of **China** increased by 5.2% in 2023, according to the first estimates of the National Bureau of Statistics of China. Although the pace of growth of the Chinese economy has been in line with Beijing's official target of around 5%, it still faces significant challenges from deflationary pressures and the real estate crisis, and investors are not enthusiastic about policies aimed at maintaining economic impulse. As of December 2023, China's industrial output increased by 6.8% compared to December 2022, retail sales increased by 7.4%, and fixed investments – up 3% for the full year 2023. China's urban unemployment rate was 5.1% in December 2023. Prices in the Chinese economy are recording their longest period of decline since 1999. The GDP deflator fell by 1.5% in October and December 2023, according to Bloomberg calculations. Another major threat remains the real estate crisis, which has affected business investment, undermined job creation and reduced consumer spending. House prices fell in December 2023 to their lowest level since 2015, while construction and finishing costs fell by 7.8% for the full year 2023. Investments in new houses, a key indicator of confidence among real estate developers, fell by 20.9% in 2023. At the same time, China's population continued its historic decline as the birth rate fell to its lowest level on record.

### 2.3 Evolution of neighbouring economies and main trading partners

In the third quarter of 2023, the gross domestic product of **Romania** increased by 0.9% (in seasonally adjusted terms) compared to the previous quarter, and compared to the same period of 2022, on a gross series basis, it increased by 2.9%. In January-November 2023, Romania's industrial production contracted by 4.8% on the gross series compared to the same period of 2022. In December 2023, consumer prices increased by 0.3% compared to the previous month and by 6.6% compared to the price level in December 2022.

In the third quarter of 2023, the gross domestic product of **Poland** decreased by 1.5% (in seasonally adjusted terms) compared to the

previous quarter, and compared to the same period of 2022, on a gross series basis it increased by only 0.8%. In January-November 2023, Poland's industrial production contracted compared to the same period of 2022 by 1.8% on the seasonally adjusted series. In December 2023, consumer prices stagnated compared with the previous month and were 6.2% higher than the price level in December 2022.

In the third quarter of 2023, the gross domestic product of **Türkiye** increased by 0.3% compared to the previous quarter (in seasonally adjusted terms) and by 5.9% compared to the similar quarter of 2022. The annual rate of inflation increased to 64.8% in December 2023, although interest rates rose significantly to 42.5% at the end of 2023. On average, the Turkish lira depreciated by 43.3% more in 2023 than in 2022. However, it is anticipated that Türkiye will achieve some stability in the coming period, which will allow for an increase in its investment rating.

In the third quarter of 2023, the economy of the **Russian Federation** grew by 1.3% (in seasonally adjusted terms) compared to the previous quarter and by 5.5% compared to the same period of 2022. In January-November 2023, the industrial output of the Russian Federation increased on an annual basis by 3.6%. Against the backdrop of the cumulative effect of the depreciation of the Russian ruble, the consumer prices in the Russian Federation continued to rise, in December 2023 they were 0.7% higher than in the previous month and 7.4% higher than in December 2022. Since July, the Bank of Russia has gradually raised the base rate from 7.5% to a cumulative level of 16.0%.

In the third quarter of 2023, the gross domestic product of **Ukraine** grew by 0.7% compared to the previous quarter (in seasonally adjusted terms) and in annual terms by 9.3%, but taking into account the destruction caused by the war, these increases are tiny to reach pre-war production volumes. At the same time, statistics and forecasts for Ukraine's economy remain bleak as the war drags on and has severely damaged industrial infrastructure and shipping. Consumer prices have followed the regional trend of moderation, with December 2023 registering a monthly inflation of 0.7%, while compared to December 2022, consumer prices in Ukraine increased by 5.1%.

## Chapter 3

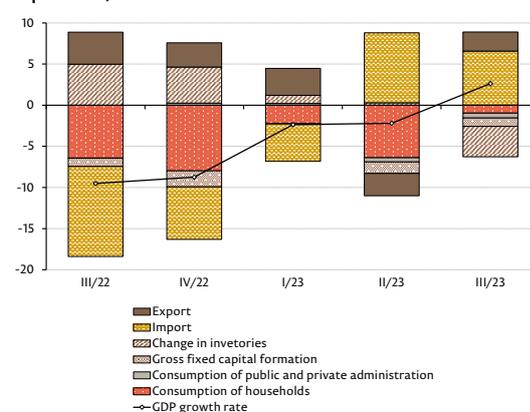
# Economic developments

### 3.1 Demand

*In the third quarter of 2023, the annual GDP dynamics returned to positive territory after the decline in the second half of 2022 and the first half of 2023. As a result, GDP increased by 2.6% compared to the same period of 2022. This dynamics was marginally higher than anticipated in the Inflation Report, November 2023. The economic activity development was mainly supported by the bountiful harvest in the agricultural sector, which created conditions for both higher exports and lower imports of agri-food products. There were also some positive developments in the financial sector, communications, social services, construction and real estate transactions. However, domestic demand continued to be modest, signaled by a fall in household consumption and investments, amid weak real income growth and heightened uncertainty in the region. Less optimistic signals regarding the economic activity are also confirmed by the negative dynamics of industry, trade and transportation, but also by a reduction in net taxes on products. At the same time, the seasonally adjusted series reflects a 0.8% decline in GDP compared to the second quarter of 2023. Overall, in the first nine months of 2023, the GDP decreased by 0.4% compared to 2022. Against this backdrop, similar to the previous periods, according to estimates, pressures from aggregate demand on prices exerted a disinflationary impact.*

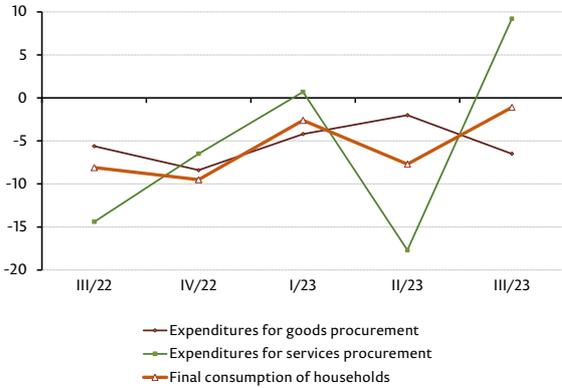
From a utilization perspective (Chart 3.1), in the third quarter of 2023, household consumption continued the decline observed in the previous periods, albeit at a more modest pace, contracting by 1.1% compared to the third quarter of 2022, generating a negative impact of 1.0 percentage points on GDP dynamics. Within the subcomponents of household consumption, the purchase of goods fell by 6.5%, while expenditure on the purchase of services increased by 9.2%. The fall in consumption was supported by the still modest development of the disposable income of the population in real terms against the background of a declining but still high inflation and an appreciating exchange rate. In the third quarter of 2023, the final consumption of public administration decreased by 2.1%, generating a negative impact of 0.3 percentage points on GDP dynamics. Gross capital formation during the reference period generated a negative impact of 4.7 percentage points on GDP dynamics. In structure, it was determined by the negative contribution from the subcomponent change in stocks (-3.7 percentage points), but also from gross fixed capital formation (-1.0 percentage points). The latter, in the context of continued heightened uncertainty in the region and tight credit conditions, recorded a contraction of 4.3% compared to the third quarter of 2022. Within this, investment in buildings and special constructions increased by 3.5%, while investment in machinery and equipment contracted by 21.5%, while the "other" subcomponent increased by 3.9%. Against the backdrop of the bumper harvest in agriculture, exports in real terms increased by 6.4% and generated a positive impact of 2.3 percentage points. A pronounced positive impact (6.6 percentage points) on GDP dynamics in the third quarter of 2023, which mitigated the above-mentioned negative contributions, was driven by a 9.8% decline in imports.

Chart 3.1: Contribution of demand components to GDP growth (percentage points)



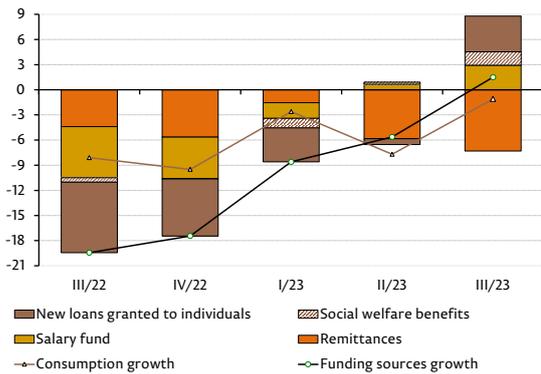
Source: NBS, NBM calculations

Chart 3.2: Developments in household final consumption in real terms (% , compared to the previous year)



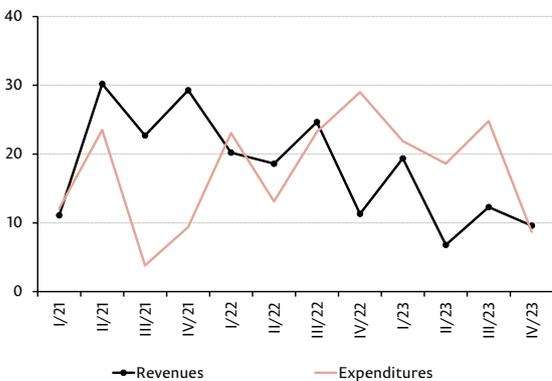
Source: NBS

Chart 3.3: Development of disposable income of the population (% , compared to the previous year) and subcomponents' contributions (percentage points)



Source: NBS, NBM calculations

Chart 3.4: Public revenue and expenditure dynamics (% , compared to the previous year)



Source: Ministry of Finance

### Household demand for consumption

**The negative annual dynamics of household consumption moderated in the third quarter of 2023.**

Thus, the annual growth rate of household final consumption registered a level of -1.1%, being 6.6 percentage points higher than in the second quarter of 2023. The respective dynamics of population consumption was supported by an increase in expenditure for the purchase of services by 9.2%. At the same time, expenditure on the purchase of goods decreased by 6.5% compared to the same period of the previous year (Chart 3.2).

**From the perspective of the main sources of consumption financing, the negative dynamics of consumption was mainly driven by the fall in real terms of remittances.**

In this regard, remittances in USD in the third quarter of 2023 contracted by 14.4% compared to the same period of the previous year, causing a pronounced negative impact (Chart 3.3) on the sources of financing consumption, which was exacerbated by the appreciation trend of the exchange rate, as well as by the increase in prices. For the month of November 2023, transfers to individuals decreased by 12.8% annually.

**On the other hand, the increases in the wage fund, social benefits and lending have had a positive impact on the main sources of financing consumption and have created the preconditions for a moderation in the negative rate of consumption over the reference period.**

### Public sector

According to the data provided by the Ministry of Finance, during the fourth quarter of 2023, the national public budget revenues amounted to MDL 28.4 billion, up by 9.6% compared to the same period of 2022 (Chart 3.4). The major share of budget revenues was accrued from taxes and fees, which accounted for 60.4%. Compulsory state social insurance contributions and mandatory health care insurance premiums accounted for 28.2%, and the share of other revenues and grants amounted to 4.5% and 7.0% of total budget revenues, respectively.

National public budget expenditures in the fourth quarter of 2023 totaled MDL 35.8 billion, registering an increase of 8.7% compared to the same period of 2022. Out of total expenditures, the largest share was spent on social protection – 31.4%, education – 17.6%, and health protection – 13.5%.

It should be noted that during the reporting period, transfers from the state budget (SB) to the state social insurance budget (SSIB), to the mandatory health insurance fund (MHIF) and to local budgets (LB) were made in the amount of MDL 13.1 billion, up by 16.6% compared to the same period of 2022 (Chart 3.5). The major share of transfers was directed to local budgets – 51.2% of total transfers, transfers to MHIF accounted for about 26.2%, with SSIB receiving 22.6% of funding.

In this context, in the fourth quarter of 2023, the execution of the national public budget resulted in a deficit of MDL 7.3 billion. In the similar period of 2022, the execution of the national public budget resulted in a deficit of MDL 7.0 billion. The balances of the national public budget accounts as of December 31, 2023 amounted to MDL 7.6 billion.

In the fourth quarter of 2023, the single treasury account (STA) was characterized by annual growth rates of transfers to the account and payments, but much lower compared to the previous quarter (Chart 3.6). As a result of inflows and outflows, at the end of 2023, the STA balance totaled around MDL 9.4 billion, registering an annual increase of 41.1% (Chart 3.7). At the same time, at the end of 2023, the balance of the Government's foreign currency deposit account with the National Bank of Moldova was the equivalent of MDL 1.3 billion, compared to MDL 2.3 billion on December 31, 2022.

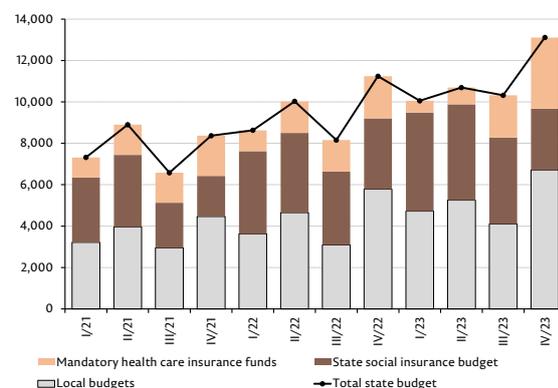
### State debt

As of December 31, 2023, the balance of state debt of the Republic of Moldova amounted to about MDL 104.0 billion, in relation to GDP<sup>16</sup> it amounted to 33.6% (Chart 3.9). In annual terms, the state debt recorded a nominal increase of 9.9% (Chart 3.8), as a result of the increase in internal state debt (with a positive contribution of 5.5 percentage points) and external state debt recalculated in national currency (with a positive contribution of 4.4 percentage points). State debt was made up of 61.9% external state debt and 38.1% internal state debt.

As of December 31, 2023, the balance of external state debt totaled about USD 3,696.2 million, higher than at the end of December 2022 by USD 555.6 million or 17.7%. Recalculated in national currency, the balance of external state debt amounted to about MDL 64.3 billion (20.8% in GDP<sup>16</sup>), (Chart 3.9).

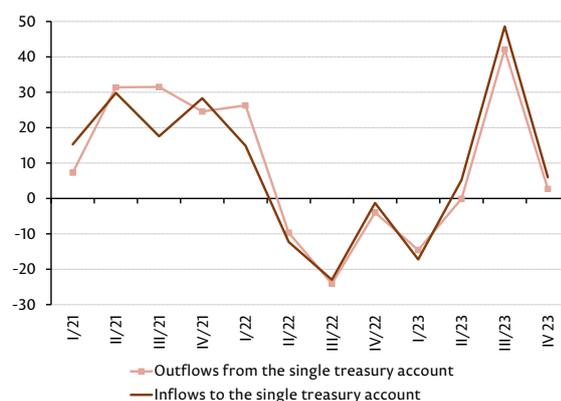
At the end of 2023, internal state debt amounted to about MDL 39.7 billion (12.8% in GDP<sup>16</sup>), (Chart 3.9), higher than that as of December 31, 2022 by 15.0% (Chart 3.8). The increase in internal government debt was driven by state securities (SS) issued on the primary market, the volume of which increased by 27.7%. As a result of these developments, internal debt consisted of SS issued on the primary market (65.0%), SS issued for the enforcement of state guarantees (29.6% of the total) and converted SS (5.4%).

Chart 3.5: Development of budgetary transfers (MDL million)



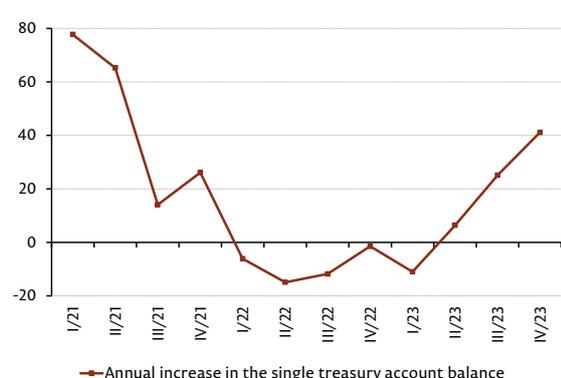
Source: Ministry of Finance

Chart 3.6: Development of the single treasury account flows (% , compared to the previous year)



Source: NBM

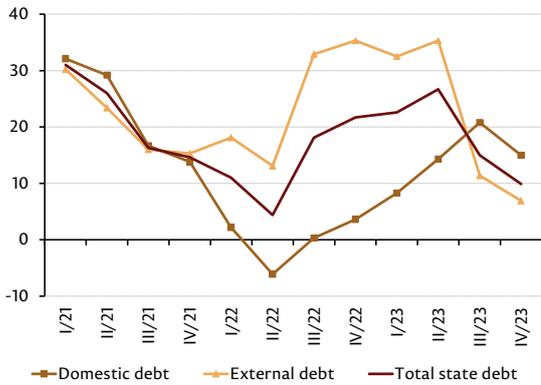
Chart 3.7: Development of the single treasury account balance (% , compared to the previous year)



Source: NBM

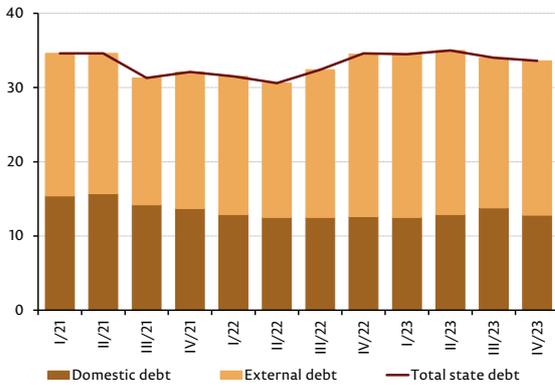
<sup>16</sup>GDP estimated by the NBM.

Chart 3.8: Development of the annual growth rate of state debt (% , end of quarter)



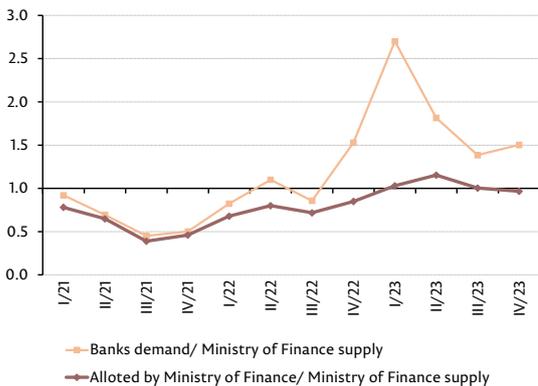
Source: Ministry of Finance

Chart 3.9: Share of state debt in GDP (% , end of quarter)



Source: Ministry of Finance

Chart 3.10: Supply and demand ratio on the primary market for state securities



Source: NBM

**Primary market of state securities (SS)**

During the fourth quarter of 2023, the Ministry of Finance put into circulation state securities totaling MDL 8,920.4 million, 3.4% less than the initial supply volume. Compared to the previous quarter, on the primary market of state securities, there was an increase, but insignificant, in demand from licensed banks (Chart 3.10). Banks' demand was 50.3% higher than the Ministry of Finance's supply, amounting to MDL 13,870.2 million.

During the reporting period, the average effective interest rates on 91-day, 182-day and 364-day maturity treasury bills declined from the level recorded in the previous quarter by 1.0 percentage points, 0.6 percentage points and 0.5 percentage points, respectively. Average effective interest rates on government bonds with a maturity of 2 and 3 years declined compared with the third quarter of 2023 by 0.3 percentage points. As regards government bonds with a maturity of 5 and 7 years, the average effective interest rates decreased by 0.3 percentage points and 0.9 percentage points, respectively, compared to the previous quarter.

During this period, banks maintained their tendency to invest in short-term securities, being more reserved towards long-term bonds, in particular those with maturities of 5 and 7 years (Chart 3.11).

The structure of the portfolio of SS put into circulation during the reference period shows that the most demanded SS were those with a maturity of 364 days, which accounted for 49.3% of total transactions, followed by 182-day treasury bills, whose share amounted to 41.9%, and the share of 91-day treasury bills accounted for 5.9%. It should be noted that the share of government bonds with a maturity of 2 years amounted to 1.5%, the share of government bonds with a maturity of 3 years – 0.9%, and the share of government bonds with a maturity of 5 and 7 years was 0.3% (Chart 3.12).

## Investment demand

**In the third quarter of 2023, the investment component generated a negative contribution of -4.7 percentage points to the dynamics of economic activity.**

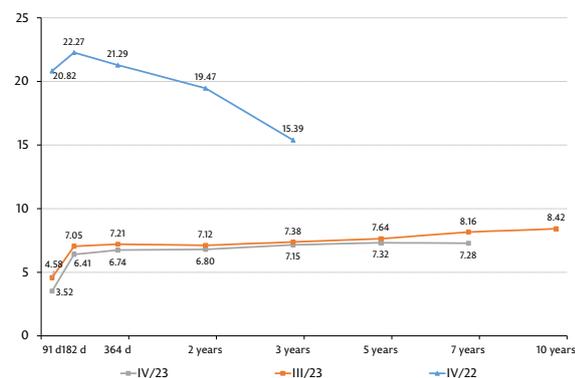
This development was driven by the negative contribution of -1.0 percentage points caused by the -4.3% decrease in gross fixed capital formation in the third quarter of 2023 compared with the same period of the previous year. This was exacerbated by the negative impact of -3.7 percentage points from the change in stocks subcomponent. The negative dynamics in gross fixed capital formation were supported by a 21.5% contraction in investment in machinery and equipment. At the same time, investment in "buildings and special constructions" increased by 3.5% (Chart 3.13). It should be noted that after a period of about two years of negative dynamics, the annual rate of construction-oriented investments returned to positive territory. However, this effect was overshadowed by the sharp contraction of the "machinery and equipment" component.

Similar to previous periods, negative investment dynamics were underpinned by subdued demand on the background of the significant increase in construction material prices in previous periods, uncertainty in the region, but also tight lending conditions.

According to the operational data presented by the NBS, investment in fixed assets increased by 2.0% in the third quarter of 2023. In structure, by type of fixed assets, the subcomponents of investment in fixed assets that drove the increase were: "machinery, equipment and installations" – by 3.1 percentage points, "other tangible fixed assets" (1.6 percentage points), "engineering constructions" (0.9 percentage points) and "intangible fixed assets" (0.9 percentage points). At the same time, negative contributions were generated by the subcomponents "residential buildings" by -2.2 percentage points, "means of transportation" by -2.1 percentage points and "non-residential buildings" by -0.2 percentage points (Chart 3.14).

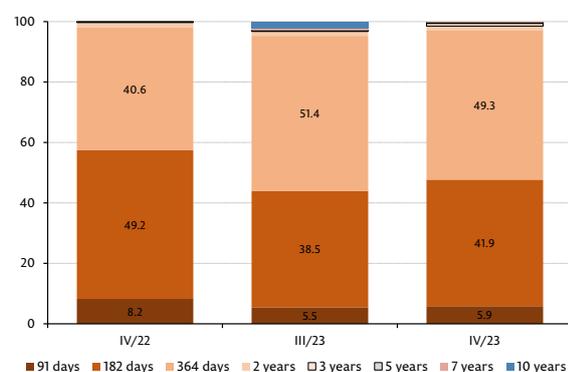
From the perspective of sources of financing investment in fixed assets for the third quarter of 2023, the positive dynamics of 2.0% was supported by the state budget (4.4 percentage points), foreign investors' funds (0.3 percentage points) and budgets of administrative-territorial units (by 3.2 percentage points). A negative impact was determined by "own funds" -3.5 percentage points and "other sources" -2.4 percentage points (Chart 3.15).

Chart 3.11: SS yield curve (%)



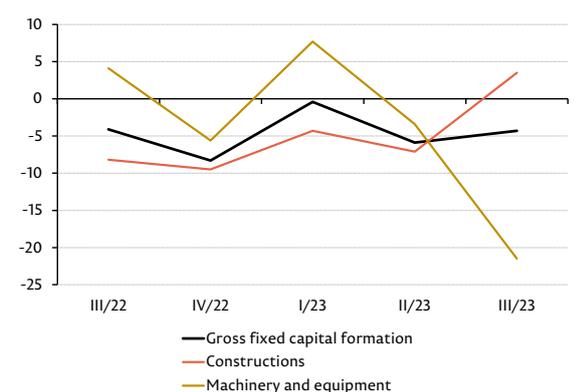
Source: NBM

Chart 3.12: Structure of SS allocated on the primary market (%)



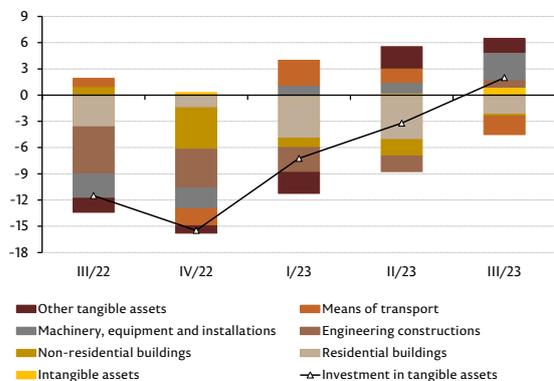
Source: NBM

Chart 3.13: Annual investment dynamics (%)



Source: NBS

Chart 3.14: Annual investment dynamics by type of fixed assets (% , real terms)



Source: NBS, NBM calculations

## Net external demand<sup>17</sup>

**The good harvest in the second half of 2023 created favorable preconditions for the export of agri-food products, which had a major effect on export dynamics. Modest internal demand, however, led to negative import dynamics. The mineral products subcomponent continued to have a significant impact on both exports and imports.**

The annual export rate in the third quarter of 2023 was -1.4% or 19.7 percentage points higher than in the second quarter of 2023. However, data for the first two months of the fourth quarter of 2023 put the annual rate of exports at a higher level (1.9%). The revival of the annual rate of exports in the second half of 2023 was driven by the increase in exports to EU countries (Chart 3.16). At the same time, exports to CIS and "Rest of the World" generated a negative impact on the dynamics of total exports.

International trade-related operational data for the first two months of the fourth quarter of 2023 show signs of a revival in exports, with exports up by 6.7% in nominal terms for November 2023. Thus, the recovery of the agricultural sector after the pronounced contraction in 2022 has been instrumental in boosting agri-food exports. At the same time, the contraction in exports of mineral products is mainly associated with the decline in international market prices of mineral products, expressed in USD (Chart 3.17).

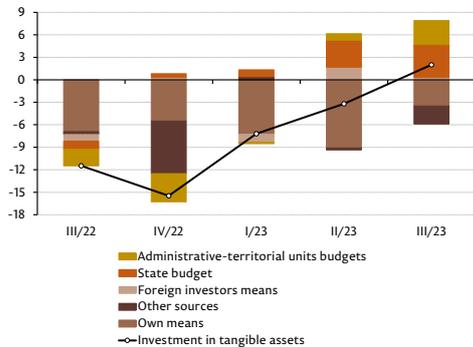
Analyzing the development of exports by product origin, it can be seen that in the last three quarters the positive effect generated by re-exports disappeared. At the same time, in the second half of 2023, the exports of domestic products generated a positive contribution to the dynamics of total exports, thus outlining reasonable premises for their revival in the next period (Chart 3.18).

In the third quarter of 2023, the annual rate of imports amounted to -14.5%, 3.9 percentage points lower than in the second quarter of 2023. At the same time, data for the first two months of the fourth quarter of 2023 still outline a pronounced negative dynamic, with imports for November 2023 down by 14.7% in annual terms. Structurally, the second semester of 2023 shows a contraction in imports from CIS and EU countries. At the same time, imports from countries classified as "Rest of the World" generated a marginal positive contribution to the dynamics of total imports (Chart 3.18).

By commodity groups (Chart 3.19), the sharp contraction of the annual rate of imports in the second half of 2023 was influenced by the dynamics of imports of "mineral products" (Chart 3.20).

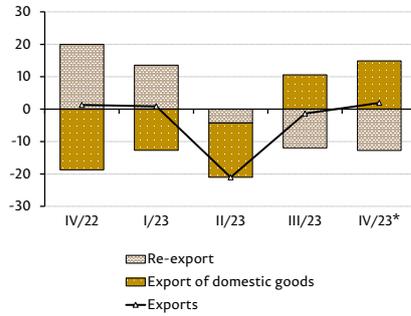
<sup>17</sup>Quarterly data on the development of international merchandise trade of the Republic of Moldova, expressed in thousands of US dollars, have been used.

Chart 3.15: Annual investment dynamics by funding sources (% in real terms)



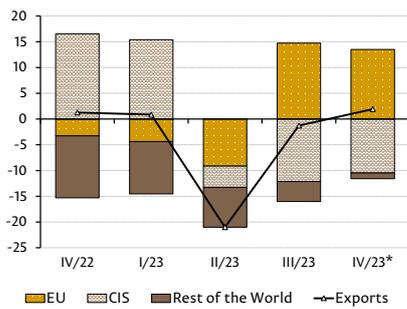
Source: NBS, NBM calculations

Chart 3.18: Development of the annual rate of exports (%) and contribution by origin (percentage points)



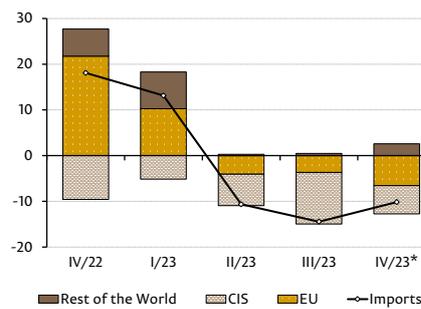
Source: NBS, NBM calculations  
\*October-November

Chart 3.16: Development of the annual rate of exports (%) and contribution by categories of countries (percentage points)



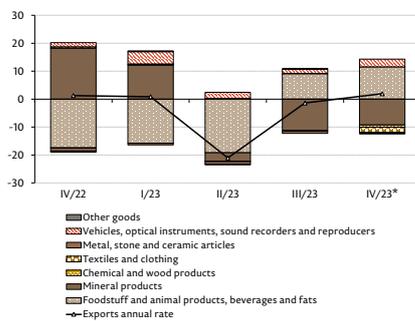
Source: NBS, NBM calculations  
\*October-November

Chart 3.19: Development of the annual rate of imports (%) and contribution by categories of countries (percentage points)



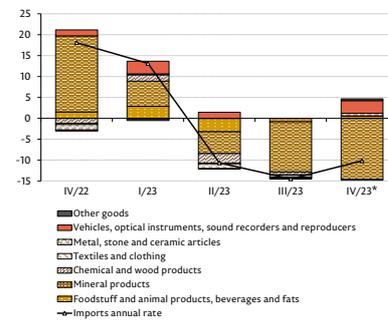
Source: NBS, NBM calculations  
\*October-November

Chart 3.17: Development of the annual rate of exports (%) and contribution of the components by commodity groups (percentage points)



Source: NBS, NBM calculations  
\*October-November

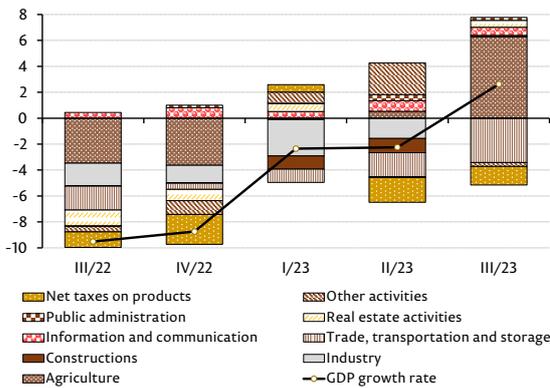
Chart 3.20: Development of the annual rate of imports (%) and contribution of the components by commodity groups (percentage points)



Source: NBS, NBM calculations  
\*October-November

### 3.2 Production

Chart 3.21: Contribution of economy sectors to GDP growth (percentage points)

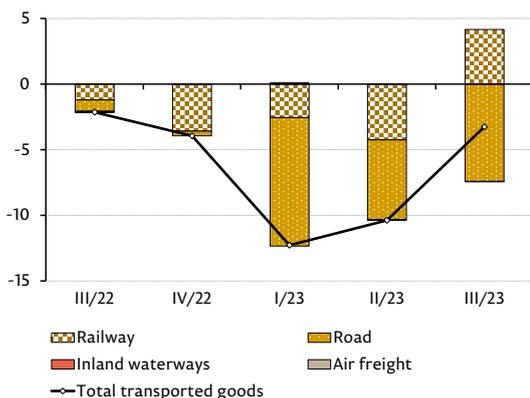


Source: NBS, NBM calculations

**By resource categories, the GDP growth in the third quarter of 2023 was mainly driven by favorable agro-meteorological conditions that supported the increase in gross value added (GVA) in the agricultural sector by 37.7% compared to the same period of the previous year.**

As a result, this subcomponent generated a positive contribution of 5.7 percentage points to GDP dynamics (Chart 3.21). Positive dynamics, but with a more modest impact, were also recorded in other sectors. Thus, GVA in accommodation and food activities increased by 29.8%, and that in the information and communication sector – by 11.7%. At the same time, real estate transactions increased by 9.5%, while the financial and insurance activities sector increased by 5.3%. GVA in construction increased by 1.7%, generating an impact of only 0.1 percentage points on GDP dynamics. Less optimistic signals about the economic activity are outlined by the negative dynamics of industry, trade<sup>18</sup>, and transportation, as well as a decrease in net taxes on products. In this regard, the GVA related to the trade subcomponent decreased by 17.1%, generating a negative impact of 3.0 percentage points on GDP dynamics. A negative contribution of -0.4 percentage points was determined by the decrease in GVA in transportation and storage by 9.2% compared to the third quarter of 2022. Freight transportation decreased by 3.3% in July-September 2023 compared to the same period of the previous year, while the number of transported passengers increased by 4.1%. The industry caused a negligible impact on GDP dynamics in the third quarter of 2023. Within it, the manufacturing industry increased by 0.5%, the energy industry – by 0.2%, and the mining and quarrying industry decreased by 14.0% compared to the third quarter of 2022. Net taxes on products decreased by 10.7%, generating a contribution of -1.5 percentage points to GDP dynamics.

Chart 3.22: Development of freight transport (% , compared to the previous year)



Source: NBS

#### Freight and passenger transport

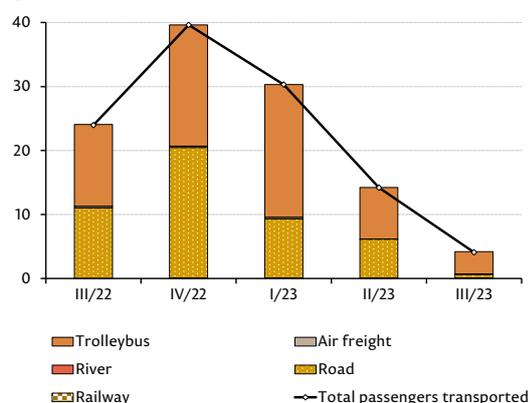
**The annual rate of the volume of freight transported in the third quarter of 2023 recorded a level of -3.3%, 7.1 percentage points higher than in the second quarter of 2023** (Chart 3.22).

This development was driven by a year-on-year decrease in the volume of freight transported by road and air by 9.0 and 15.1%, respectively, compared to the same period of the previous year. At the same time, the volume of freight transported by inland waterways decreased by 1.6%, while the volume of freight transported by rail increased by 24.0%.

<sup>18</sup>Wholesale and retail trade; maintenance and repair of motor vehicles and motorcycles.

Favourable results were recorded in the passenger transport sector in the third quarter of 2023. Thus, the annual rate of the number of passengers transported recorded a level of 4.1%, which was, however, 10.1 percentage points lower than in the second quarter of 2023 (Chart 3.23). This development was driven by the increase in annual terms of the number of passengers transported by road and trolleybuses by 1.8 and 5.3%, respectively, while the number of passengers transported by inland waterway increased by 74.0%. At the same time, the number of passengers transported by rail increased by 42.3%, while the number of passengers transported by air decreased by 12.6% compared to the same period of the previous year.

Chart 3.23: Passenger transport development (% , compared to the previous year)



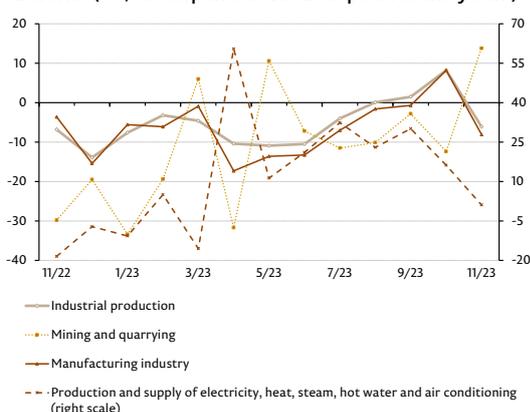
Source: NBS

## Industrial production

**In the first two months of the fourth quarter of 2023, the annual growth rate of the volume of industrial production registered an average level of 1.1%, 1.9 percentage points higher than in the third quarter of 2023** (Chart 3.24).

This dynamics was driven by the intensification of the annual growth rate of the manufacturing industry (from -3.1% in the third quarter of 2023 to 0.1% in the first two months of the fourth quarter of 2023). At the same time, the mining and quarrying sector in October-November 2023 increased (from -8.1% in the third quarter of 2023 to 0.7% in the first two months of the fourth quarter of 2023), while the annual growth rate of the volume of production in the sector "production and supply of electricity, heat, steam, hot water and air conditioning" decreased by 19.9 percentage points compared to the third quarter of 2023, to the level of 8.7%.

Chart 3.24: Industry development in real terms (% , compared to the previous year)



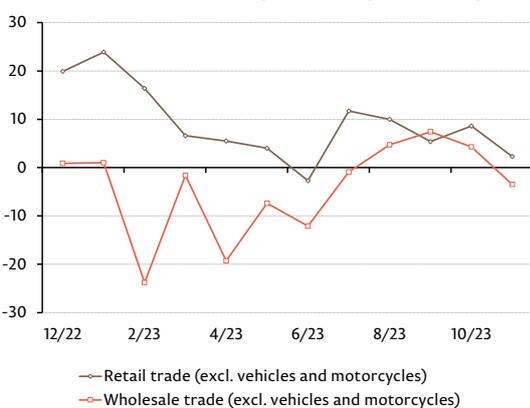
Source: NBS

## Internal trade

**In the first two months of the fourth quarter of 2023, internal retail trade (based on VAT statements<sup>19</sup>) recorded an average increase of 5.5%, a rate 3.6 percentage points lower than in the previous quarter** (Chart 3.25).

At the same time, internal wholesale trade (based on VAT statements) recorded an average growth of 0.4% during October-November 2023, which is 3.3 percentage points lower than in the third quarter of 2023.

Chart 3.25: Internal trade (based on VAT statements) (% , compared to previous year)

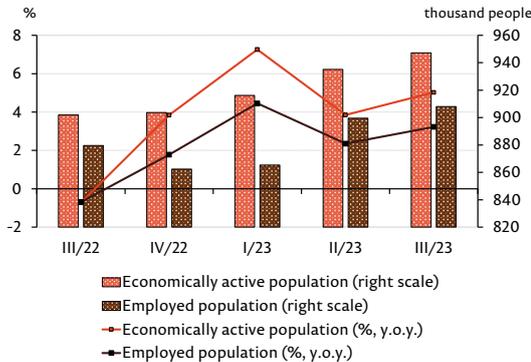


Source: NBS, NBM calculations

<sup>19</sup>[https://statistica.gov.md/ro/statistici-privind-indicii-valorici-ai-vanzarilor-livrarilor-de-marfuri-si-servi-12\\_60432.html](https://statistica.gov.md/ro/statistici-privind-indicii-valorici-ai-vanzarilor-livrarilor-de-marfuri-si-servi-12_60432.html)

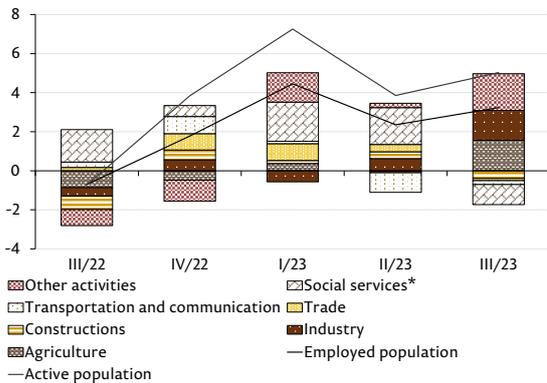
### 3.3 Labour market

Chart 3.26: Economically active population and employed population



Source: NBS, NBM calculations

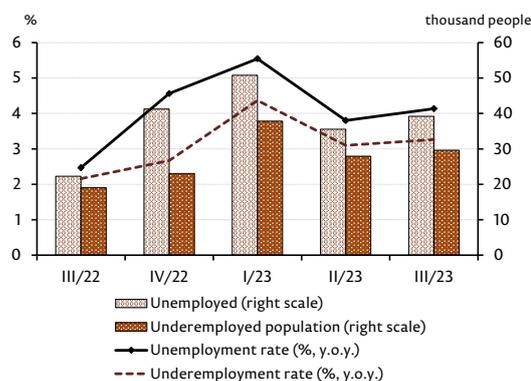
Chart 3.27: Contribution of sectors to the dynamics of employed population (percentage points)



Source: NBS, NBM calculations

\*Public administration, education, health and social assistance

Chart 3.28: Development of unemployed and underemployed population



Source: NBS, NBM calculations

#### Labour force

**The positive annual dynamics of the economically active and employed population observed in the first half of 2023 continued in the third quarter of 2023. At the same time, both the unemployment and underemployment rates<sup>20</sup> increased compared to the third quarter of 2022.**

In July-September 2023, the labour force totaled 947.1 thousand people, up by 5.0% compared to the third quarter of 2022. At the same time, the employed population amounted to 907.9 thousand people, up by 3.2% compared to the same period of 2022 (Chart 3.26).

Positive dynamics were recorded in the agricultural sector (6.9%), the industrial sector (11.5%) and other activities (24.1%). At the same time, the number of employed population declined in the third quarter of 2023 in the remaining economic sectors: trade (-0.6%), transportation and communication (-2.9%), social services (-4.5%), construction (-4.8%), (Chart 3.27).

In the third quarter of 2023, the number of unemployed was 39.2 thousand people or by 16.9 thousand people higher than in the third quarter of 2022, and the unemployment rate was 4.1%, which is 1.6 percentage points higher than in the third quarter of 2022 (Chart 3.28).

At the same time, the underemployed population also showed positive dynamics. Thus, in the third quarter of 2023, it increased to 29.6 thousand people, from 19.0 thousand people in July-September 2022, and the underemployment rate amounted to 3.3% or 1.1 percentage points higher than in the third quarter of 2022.

<sup>20</sup>Underemployed persons: persons who had a job, whose total number of hours actually worked during the reference period was less than 40 hours per week, who were willing and available to work overtime hours.

## Wage fund

**In the third quarter of 2023, the annual rate of the wage fund per economy, although decreasing compared to the previous quarter, continued to be significant and in real terms it has been on an upward trajectory.**

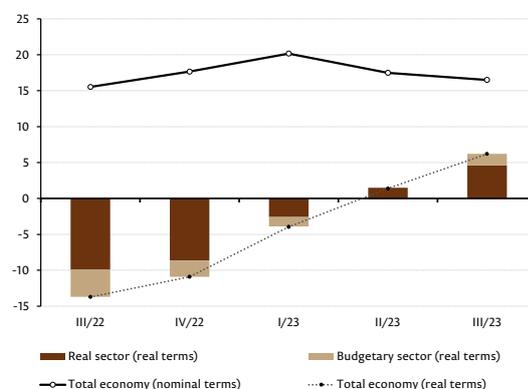
The wage fund per economy increased by 16.5% compared to the third quarter of 2022. This dynamics was mainly driven by developments in the wage fund of the trade sector, which contributed by 3.3 percentage points, the information and communication sector (2.1 percentage points), education (2.0 percentage points), health and social work (1.9 percentage points), industry (1.7 percentage points) and public administration and defense (1.5 percentage points).

However, in real terms, deflated by CPI, the wage fund per economy increased by 6.2% compared to the same period of the previous year, as a result of the development of both sectors of the economy: real and budgetary (Chart 3.29).

In the third quarter of 2023, the average number of employees at the national economy level increased by 0.4% compared to the third quarter of the previous year. The number of employees in the real sector increased by 0.8%, with a contribution of 0.6 percentage points, while the number of employees in the budget sector contracted by -0.9%, with a contribution of -0.2 percentage points (Chart 3.30).

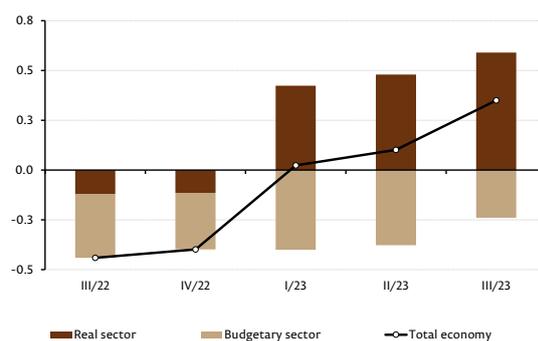
The distribution by sectors of the economy reveals more pronounced increases in the average number of employees in accommodation and food service activities (30.1%), information and communication (4.8%), wholesale and retail trade (3.7%) and agriculture (3.6%). At the same time, a contraction in the number of employees can be seen in real estate transactions (-6.2%), professional, scientific and technical activities (-4.8%), industry (-3.1%), construction (-3.0%), transportation and storage (-2.9%) and education (-1.2%), (Chart 3.31).

Chart 3.29: Wage fund in the economy (% , compared to the previous year) and sectors' contributions (percentage points)



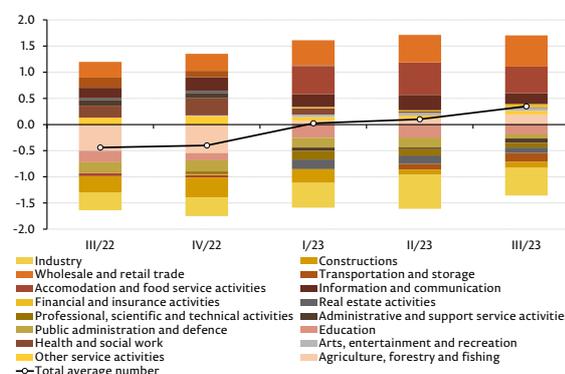
Source: NBS, NBM calculations

Chart 3.30: Average number of employees per economy (% , compared to the previous year) and sectors' contributions (percentage points)



Source: NBS, NBM calculations

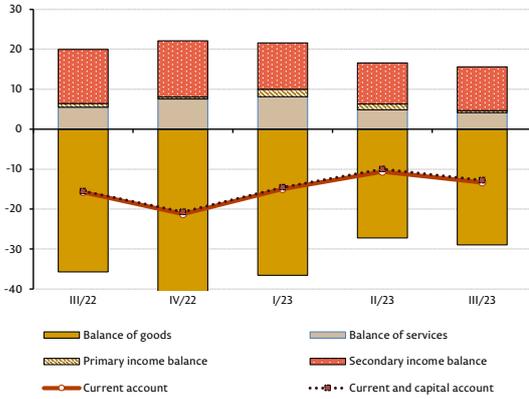
Chart 3.31: Contribution of the sectors of the economy to the dynamics of the number of employees (% , compared to the previous year)



Source: NBS, NBM calculations

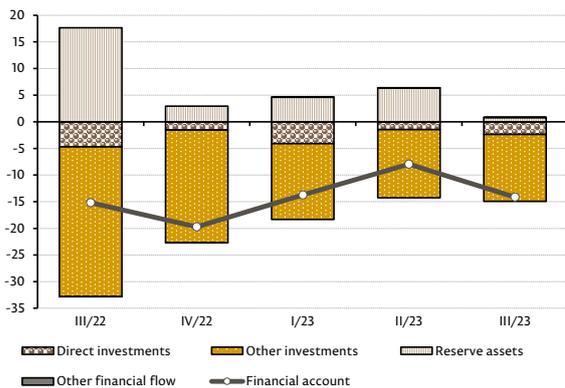
### 3.4 External sector

Chart 3.32: Current account share in GDP (%)



Source: NBM

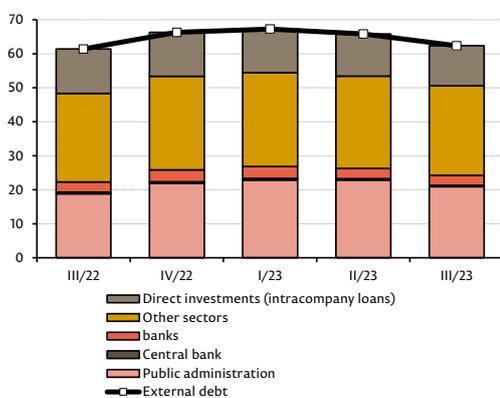
Chart 3.33: Financial account share in GDP (%)



Source: NBM

Note: (-) – net inflow of capital, (+) – net outflow of capital

Chart 3.34: External debt share in GDP (%)



Source: NBM

#### Current account

**In the third quarter of 2023, the current account deficit on the balance of payments increased by 2.7 percentage points compared to that of the previous quarter, constituting 13.3% as a share of GDP (Chart 3.32).**

The increase in the balance of payments deficit was due to an increase in the component with a negative contribution – "balance of goods". At the same time, the components with a positive contribution: "balance of primary income" and "balance of services" decreased, while the "balance of secondary income" increased during the reference period.

#### Financial account

**In the third quarter of 2023, the financial account, as a share of GDP, recorded a level of 14.1%, 6.2 percentage points higher than in the second quarter of 2023.**

At the same time, there were changes in the structure of net financial flows, but the overall picture, compared with the previous quarter, did not change fundamentally (Chart 3.33). Thus, in the third quarter of 2023, the "other investments" component recorded a prominent development, thus contributing to the significant increase in net inflows of financial assets<sup>21</sup>. It should be noted that the net inflow of direct investments as a share of GDP amounted to 2.4%, up by 0.9 percentage points compared to the second quarter of 2023. In the third quarter of 2023, there were net accumulations of reserve assets (0.8% as a share of GDP) and, as a result, there was a decrease in net capital inflows.

The share of external debt in GDP amounted to 62.4%, being 3.4 percentage points lower than in the second quarter of 2023 (Chart 3.34). There were no major changes in the external debt structure, thus similar to the previous periods, the major share in the total external debt is held by the economic agents<sup>22</sup> with 29.3%, the government sector<sup>23</sup> with 21.3% and direct investments – 11.8%.

<sup>21</sup>In the third quarter of 2023, the "cash and deposits" and "trade credits and advances" components contributed to the significant increase in net financial inflows as a component part of "other investments".

<sup>22</sup>Cumulative debt of "Banks" and "Other sectors".

<sup>23</sup>Cumulative debt of "Public administration" and "Central bank".

## Chapter 4

# Monetary policy

### 4.1 Monetary policy instruments

#### Money market interest rates development

**During the fourth quarter of 2023, the National Bank lowered the monetary policy rate from 6.00% annually to 4.75% annually. The decisions were taken in view of the further propagation of the monetary policy easing measures of the last period and aim at anchoring inflation expectations, with a view to keeping inflation within the target fluctuation range in the medium-term.**

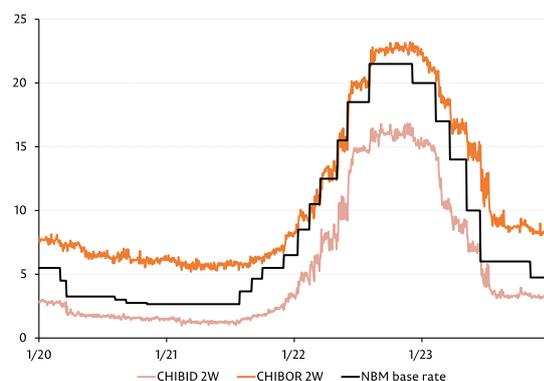
The CHIBOR yield curve remained quasi-static during the fourth quarter of 2023, with only slight changes in both directions. Thus, the CHIBOR 2W quotation at the end of December was slightly lower (-0.54 percentage points) than on the last day of the previous quarter, constituting 8.19% (Chart 4.1).

The trajectory of interest rates on government securities, both on the primary and secondary segments, reflected the signal sent by the NBM's monetary policy decisions in the previous quarter.

Thus, the interest rate on government securities with a maturity of 91 days in the last month of the fourth quarter of 2023, of 2.91%, was 0.96 percentage points lower than at the end of the third quarter of 2023.

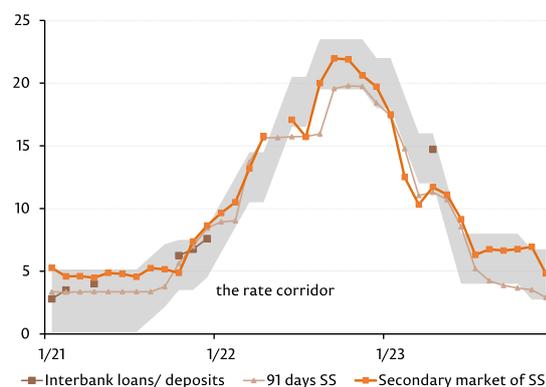
On the secondary segment of the state securities market, the interest rate on transactions amounted to 4.83% (-1.58 percentage points compared to the end of the third quarter of 2023), (Chart 4.2).

Chart 4.1: Monthly average reference rates on the interbank market and the base rate of the NBM (%)



Source: NBM

Chart 4.2: Monthly development of the interest rates corridor (%)

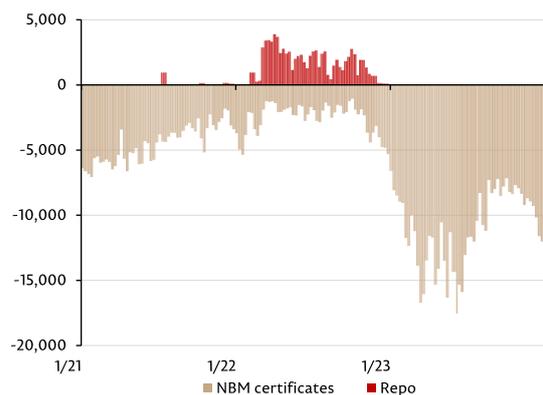


Source: NBM

## Money market operations

### **Sales of Certificates issued by the National Bank of Moldova (NBC)**

Chart 4.3: Development of the daily balance of sterilization operations (MDL million)



Source: NBM

The gradual amplification of the NBM's debtor position vis-à-vis the banking system was reflected in the evolution of the daily stock of NBC placements, ranging between the minimum value of MDL 7,153.6 million at the beginning of October and the maximum value of MDL 12,009.2 million at the end of December. This increase, however, was not reflected in the average quarterly balance, which decreased by MDL 239.0 million compared to the third quarter of 2023, amounting to MDL 9,161.2 million (Chart 4.3).

### **Repo operations**

Liquidity-providing repo operations were conducted weekly with a 14-day maturity at a fixed interest rate (base rate plus a margin of 0.25 percentage points) through a tender procedure without a ceiling. The repo operations balance at the end of the management quarter was zero.

### **Standing facilities**

During the fourth quarter of 2023, banks used both standing facilities offered by the NBM.

The total amount of overnight deposits placed with the NBM amounted to MDL 17,002.3 million, about 5.7% below the level of the previous quarter. The average daily stock of these placements decreased to MDL 266.5 million from MDL 357.8 million in the previous quarter. The amounts placed by banks ranged from a minimum of MDL 10.0 million to a maximum of MDL 1,800.0 million.

The total amount of overnight loans granted to banks by the NBM in the fourth quarter of 2023 amounted to MDL 452.0 million, down by about 3.7 times compared to the previous period. The average daily balance of overnight loans amounted to MDL 4.9 million.

During the fourth quarter of 2023, the NBM lowered the monetary policy interest rates by 1.25 percentage points, thus, as of December 31, 2023, they amounted to 2.75% on overnight deposits and 6.75% on overnight loans.

### **Required reserves**

The required reserves mechanism continued to perform monetary control and liquidity management functions in the banking system.

On November 7, 2023, the Executive Board of the NBM, in view of the maintenance of the disinflationary trends, decided to decrease the required reserve ratio from funds attracted in MDL and non-convertible currency from 34.0% to 33.0% and the required reserve ratio from funds attracted in freely convertible currency (FCC) from 45.0% to 43.0% of the calculation base. These changes have been applied with effect from December 16, 2023.

In the application period December 16, 2023 – January 15, 2024, required reserves in MDL amounted to MDL 22,840.9 million, increasing by MDL 220.2 million (+1.0%) compared to those maintained in the period September 16, 2023 – October 15, 2023.

With regard to required reserves from funds attracted in FCC, in the application period December 16, 2023 – January 15, 2024, they amounted to USD 243.8 million and EUR 638.7 million. Compared to the period September 16, 2023 – October 15, 2023, required reserves in US dollars decreased by 0.4% and reserves in euro increased by 0.1%.

### **Interventions on the domestic foreign exchange market**

The NBM intervened on the domestic foreign exchange market from October to December 2023 through foreign exchange purchases.

During the analyzed period, the volume of NBM transactions carried out on the interbank foreign exchange market against MDL, at the exchange date, amounted to USD 18.28 million, including purchase transactions in the amount of USD 17.80 million, as well as foreign exchange conversions with the World Bank institutions (International Bank for Reconstruction and Development and International Development Association) in the amount of USD 0.48 million (Chart 4.4).

## 4.2 Monetary indicators dynamics

**In the fourth quarter of 2023, the monetary aggregates recorded more moderate annual growth rates, thus the monetary aggregate M2 recorded an annual growth rate of 21.2% (5.2 percentage points lower than in the third quarter of 2023), and M3 – an annual growth rate of 18.3% (2.0 percentage points lower than in the previous quarter). The monetary base recorded a slower annual rate of growth, constituting 10.6% annually (Chart 4.5).**

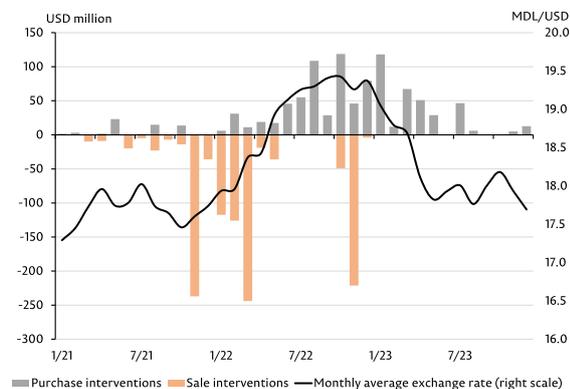
### **Money supply**

The moderation in the growth rate of the monetary aggregate M3 during the fourth quarter of 2023 was generated by the slowdown in the growth rate of deposits in national currency and currency in circulation, which boosted the growth of foreign currency deposits. All this provided the monetary aggregate M3 with an annual growth rate of 18.3% (Chart 4.6).

The moderation in the growth rate of deposits in national currency to 26.5% annually (Chart 4.8) was driven by a more modest increase in term deposits of individuals and legal entities compared to the previous quarter.

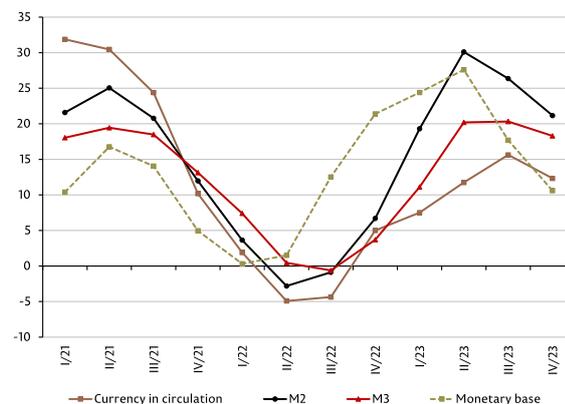
Deposits in foreign currency in the fourth quarter of 2023 registered an increase of 11.1% annually, 4.9 percentage points more than in the previous quarter, as a result of faster growth in term deposits (Chart 4.11). The 25.2% positive value of foreign currency term deposits was driven by a higher increase in the

Chart 4.4: Development of the official MDL/USD exchange rate and volume of daily transactions of the NBM



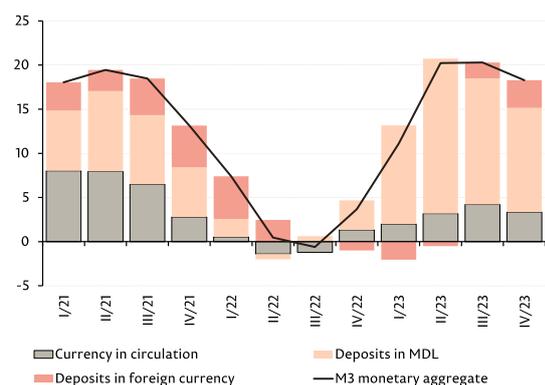
Source: NBM

Chart 4.5: Change in monetary aggregates (% annual growth)



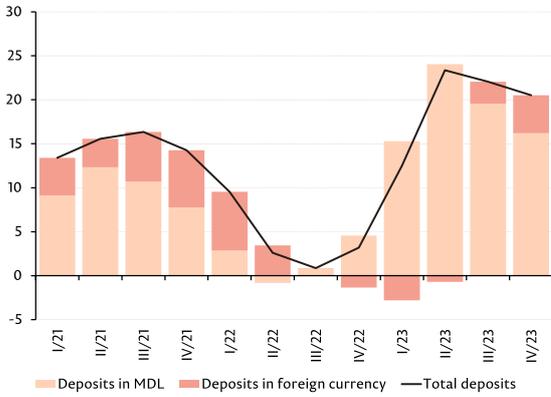
Source: NBM

Chart 4.6: Dynamics of the monetary aggregate M3 (% contribution of the components in annual growth)



Source: NBM

Chart 4.7: Dynamics of the total deposit balance (% , component contribution to annual growth)

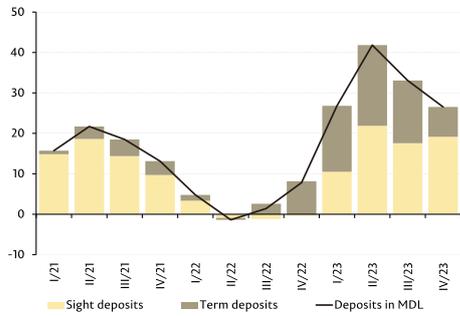


Source: NBM

contribution of deposits by individuals compared with the third quarter of 2023, but also by the contribution of deposits by legal entities (Chart 4.12). At the same time, sight deposits in foreign currency emerged from the negative range, recording a slight increase in the fourth quarter, constituting 1.5% annually, as a result of the increase in the volume of sight deposits of legal entities (Chart 4.13).

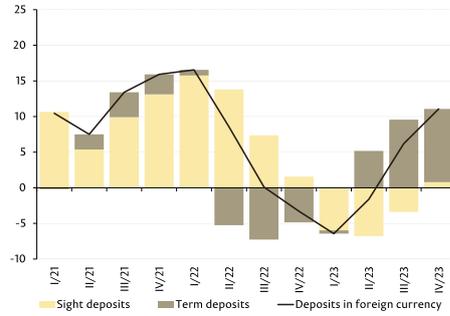
The rate of growth of money in circulation in the fourth quarter of 2023 slowed by 3.3 percentage points compared to the previous quarter, constituting 12.3% annually. The quarterly average contribution of money in circulation to M3 growth declined by 0.9 percentage point compared to the third quarter of 2023 (Chart 4.6). The dynamics of money in circulation were driven by both receipts and releases from commercial banks' vaults. Of the total receipts, receipts from the sale of consumer goods accounted for the largest share. At the same time, as regards releases from commercial banks' vaults, the main components were releases from ATMs and POS terminals.

Chart 4.8: Dynamics of the balance of deposits in MDL (% comp. contrib. in annual growth)



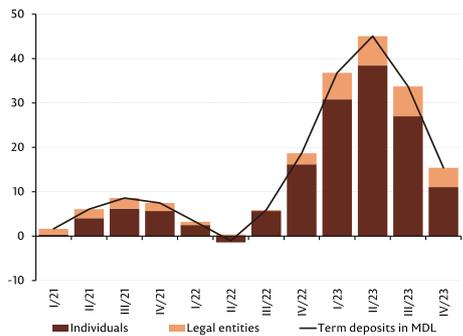
Source: NBM

Chart 4.11: Dynamics of the balance of deposits in foreign currency (% comp. contrib. in annual growth)



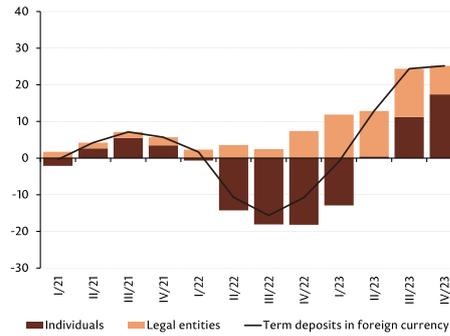
Source: NBM

Chart 4.9: Dynamics of the term deposits balance in MDL (% comp. contrib. in annual growth)



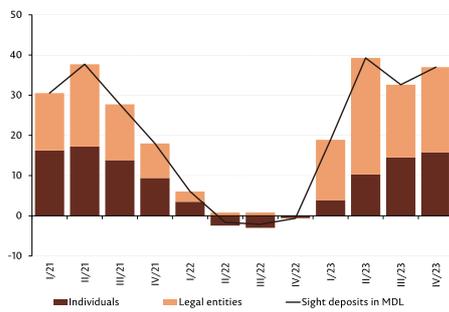
Source: NBM

Chart 4.12: Dynamics of the term deposits balance in foreign currency (% comp. contrib. in annual growth)



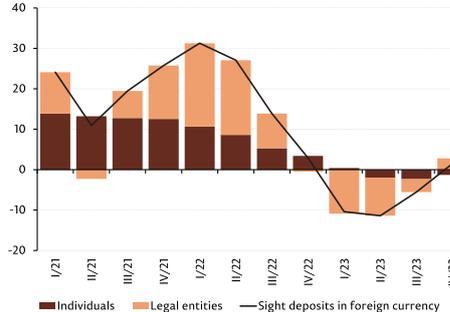
Source: NBM

Chart 4.10: Dynamics of the sight deposits balance in MDL (% comp. contrib. in annual growth)



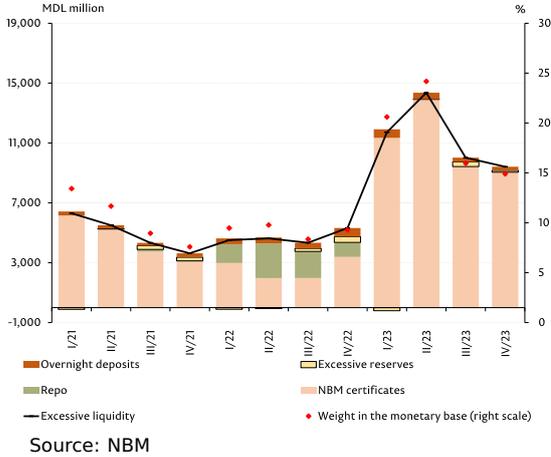
Source: NBM

Chart 4.13: Dynamics of the sight deposits balance in foreign currency (% comp. contrib. in annual growth)



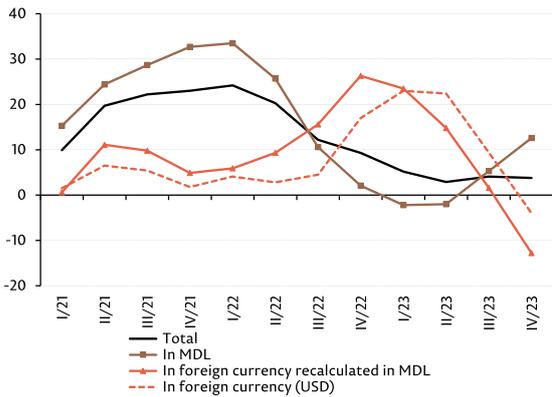
Source: NBM

Chart 4.14: Excess liquidity



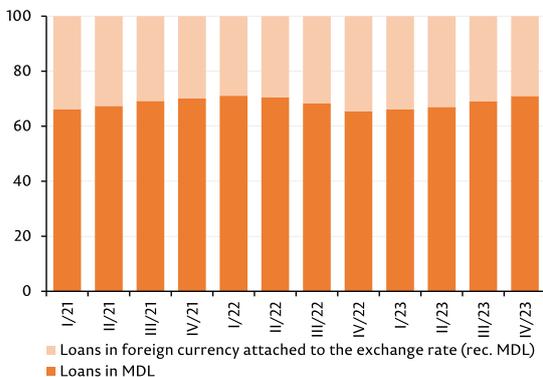
Source: NBM

Chart 4.15: Development of loans balance (% annual growth)



Source: NBM

Chart 4.16: Development of loans shares, by subcomponents in the total balance (%)



Source: NBM

### Excess liquidity

During the fourth quarter of 2023, the average excess liquidity in the banking system decreased by MDL 603.5 million. It should be noted that, compared with the fourth quarter of 2022, the volume of excess liquidity increased by MDL 4.0 billion, registering an average value of MDL 9.4 billion (Chart 4.14).

In January 2024, excess liquidity amounted to MDL 12.7 billion on average.

### Credit market

#### Development of loans balance granted by licensed banks<sup>24</sup>

At the end of December 2023, the total balance of loans granted by the licensed banks recorded an annual increase, amounting to MDL 61,923.1 million, 3.8% higher than at the end of the fourth quarter of 2022 (Chart 4.15). The increase was boosted only by the component in national currency, which continued its upward trend, reaching 12.6%. The annual trajectory of the balance of loans granted in MDL was influenced by the increase in the balance of loans granted to legal entities by 18.0% and in those granted to individuals by 9.0%. The increase in the balance of the MDL component also increased the share of this component. Thus, the balance of loans granted in MDL amounted to 71.0% of the total balance of loans, 5.5 percentage points higher than at the end of 2022 (Chart 4.16). It should be noted that the annual rate of the balance of loans in foreign currency and pegged to the exchange rate recorded negative values (Chart 4.15).

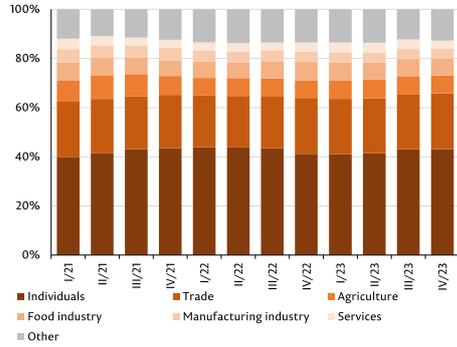
At the end of the fourth quarter of 2023, in the structure of the total portfolio of loans granted by the licensed banks, the largest share, analogous to the previous quarters, was accounted for by loans granted to individuals (43.1%), followed by the share of loans granted to legal entities in the trade sector (22.7%), (Chart 4.17).

#### Development of new loans granted by the licensed banks

Over the fourth quarter of 2023, the annual dynamics of the total volume of new loans granted by the licensed banks amounted to 15.5% (Chart 4.18), as lending in MDL increases. The development of new loans granted in MDL recorded an annual growth rate of 39.3%, as a result of the increase in loans granted to both legal entities and individuals (Chart 4.19), due to the continuous decrease in interest rates (Chart 4.23). The major contributions came from the increase in loans granted to both individuals for consumption and real estate, as well as to legal entities in the trade sector. The share of loans granted in domestic currency in the fourth quarter of 2023 amounted to 74.8% of total loans granted, compared to 62.0% in the fourth quarter of 2022. At the same time, new loans granted in foreign currency and pegged to the foreign exchange rate, analogous to the previous quarters, recorded negative annual rates (Chart 4.18).

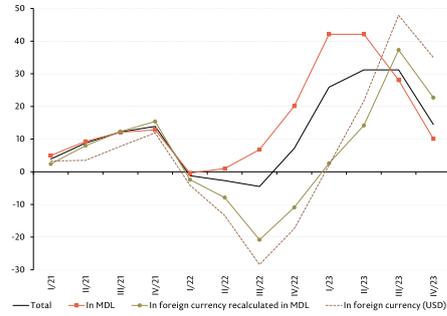
<sup>24</sup>Data analysis was based on the reports ORD 01.06 "Interest rates on loans and deposits balance" submitted by the licensed banks by January 11, 2024.

Chart 4.17: Loan balance structure (% in total)



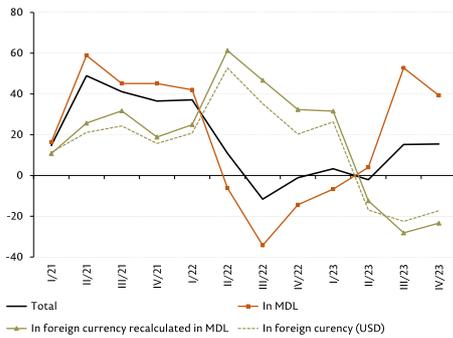
Source: NBM

Chart 4.20: Deposit balance dynamics (% annual growth)



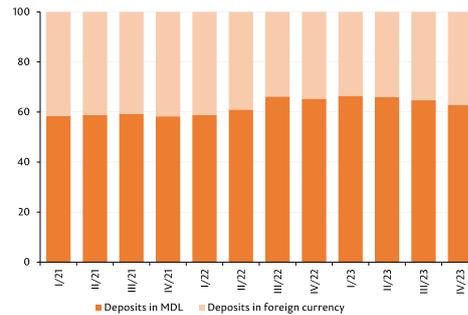
Source: NBM

Chart 4.18: Evolution of new granted loans (% annual growth)



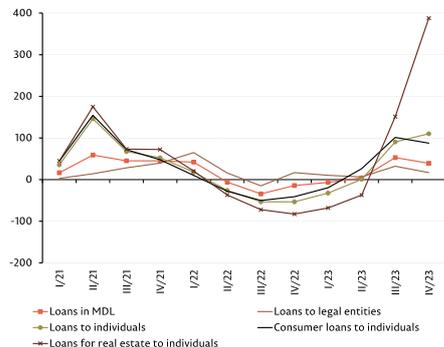
Source: NBM

Chart 4.21: Evolution of the share of term deposits on subcomponents in the total balance (%)



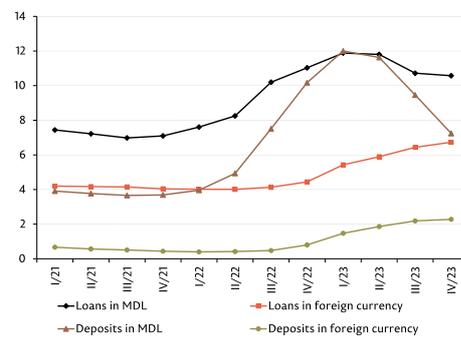
Source: NBM

Chart 4.19: Evolution of new granted loans in MDL (% annual growth)



Source: NBM

Chart 4.22: Average interest rates on balance of loans and deposits (%)



Source: NBM

### ***The market of term deposits accepted by the licensed banks (deposits balance)<sup>25</sup>***

At the end of the reporting quarter, the total balance of term deposits attracted by the licensed banks amounted to MDL 45,506.5 million. The annual growth rate was 14.5%, lower than at the end of the previous quarter (Chart 4.20). The MDL component recorded an annual growth rate of 10.1%, as new term deposits decreased as a result of the continuous cuts in interest rates. The share of the balance of term deposits in MDL declined to 62.9% compared to 65.3% at the end of the fourth quarter of 2022 (Chart 4.21). The annual change in the balance of foreign currency deposits, recalculated in MDL, also declined.

### **Interest rates<sup>26</sup>**

#### ***Base rate development***

During the fourth quarter of 2023, two meetings of the Executive Board of the National Bank of Moldova were held on monetary policy decisions. Following the assessment of the balance of internal and external risks and the short- and medium-term inflation outlook, the Executive Board of the National Bank of Moldova, at its meeting on November 7, 2023, decided to lower the base rate applied to the main monetary policy operations by 1.25 percentage points to 4.75% annually, and subsequently, on December 14, 2023, maintained this level. These measures were adopted with the aim of easing inflationary pressures, stimulating aggregate demand, including by encouraging consumption, balancing the national economy and anchoring inflationary expectations. The decisions aim to anchoring inflation expectations, keeping the inflation rate close to the target of 5.0% over the medium-term, with a possible deviation of  $\pm 1.5$  percentage points.

#### ***Interest rate development on loans balance***

For the period October-December 2023, the weighted average interest rate related to the balance of loans granted in MDL by the licensed banks decreased compared to the fourth quarter of 2022 by 0.46 percentage points and amounted to 10.57% annually (Chart 4.22), as a result of the cuts in interest rates on new transactions. The weighted average interest rate related to the balance of loans granted in foreign currency continued to increase and amounted to 6.73% annually, 2.29 percentage points higher than in the fourth quarter of 2022.

#### ***Deposit balance interest rate development***

Over the reporting quarter as a whole, the weighted average interest rate related to the balance of term deposits in national currency decreased more sharply than in the loans segment (Chart 4.22). The weighted average interest rate related to the balance of term deposits in national currency amounted to 7.24% annually,

<sup>25</sup>Data analysis was based on the reports ORD 01.06 "Interest rates on loans and deposits balance" submitted by the licensed banks until January 11, 2024 and does not include sight deposits.

<sup>26</sup>The analysis of rates has been carried out on the basis of the reports ORD 01.06 "Interest rates on loans and deposits balance" submitted by the licensed banks until January 11, 2024 and does not include rates on sight deposits.

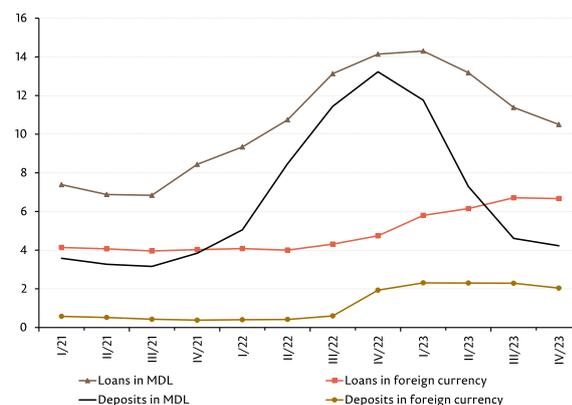
2.93 percentage points lower than in the fourth quarter of 2022. At the same time, the weighted average interest rate related to the balance of term deposits in foreign currency amounted to 2.28% annually, higher than in the fourth quarter of 2022.

### **Development of interest rates on new loans and deposits granted/ attracted by the licensed banks**

In the fourth quarter of 2023, in the domestic currency segment, weighted average interest rates on new loans granted and term deposits continued to decline (Chart 4.23), including under the impact of the pass-through mechanism of the consecutive base rate cuts applied to the main monetary policy operations that started in December 2022. Over the quarter as a whole, the weighted average interest rate on MDL deposits amounted to 4.23% annually, 9.0 percentage points lower than in the fourth quarter of 2022 (Chart 4.23). The weighted average interest rate on term deposits attracted in national currency from individuals (-10.86 percentage points compared to the fourth quarter of 2022) decreased even more sharply and amounted to 4.29% annually. In addition, the weighted average interest rate on term deposits attracted from legal entities decreased and amounted to 4.07% annually.

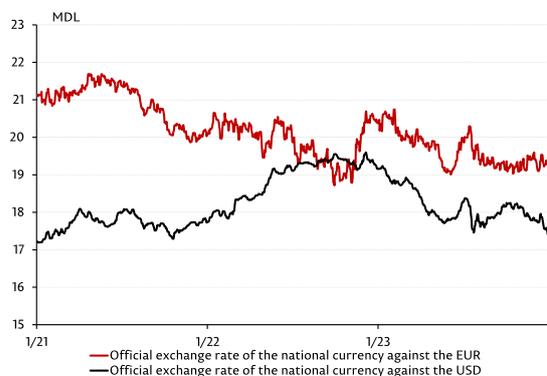
In the fourth quarter of 2023, the weighted average interest rate on new loans granted in national currency amounted to 10.50% annually, 3.64 percentage points lower than in the fourth quarter of 2022. The decline reflected the decrease in the weighted average interest rate on loans to both individuals (-4.64 percentage points) and legal entities (-3.52 percentage points) compared to the fourth quarter of 2022. At the same time, the weighted average interest rate on loans granted in foreign currency and pegged to foreign exchange rates amounted to 6.67% annually, 1.93 percentage points higher than in the fourth quarter of 2022.

Chart 4.23: Average interest rates on new volumes of loans and deposits (%)



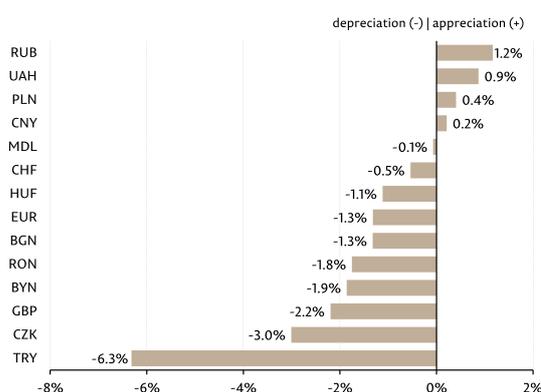
Source: NBM

Chart 4.24: Fluctuations of the official exchange rate of the Moldovan leu against the US dollar and the euro



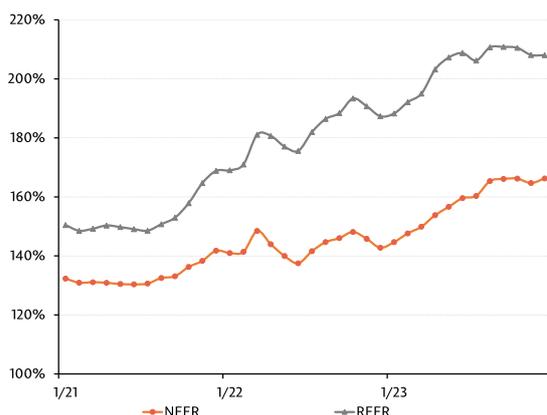
Source: NBM

Chart 4.25: Development of the currencies of countries – main trading partners of the Republic of Moldova, in relation to the US dollar, average exchange rate in the fourth quarter of 2023/ third quarter of 2023 (%)



Source: NBM

Chart 4.26: Dynamics of the nominal effective exchange rate (NEER) and real effective exchange rate (REER) of the MDL calculated on the basis of the weight of the countries – main trading partners (Dec.2000-100%)



Source: NBM

### Nominal and real effective exchange rate development

According to the values at the end of the fourth quarter of 2023, the nominal official exchange rate of the national currency appreciated by 4.1% against the US dollar, while against the euro it depreciated by 1.2% compared to their levels recorded at the end of the previous quarter (Chart 4.24).

On average, the exchange rate of the Moldovan leu depreciated against the US dollar by 0.1% and appreciated against the euro by 1.2%, compared to the averages of the previous quarter.

As regards the development of the currencies of countries – main trading partners of the Republic of Moldova, in the fourth quarter, most of the currencies recorded more pronounced depreciations against the US dollar, compared to the 0.1% depreciation of the Moldovan leu, especially the Turkish lira (-6.3%), the Czech koruna (-3.0%), the pound sterling (-2.2%). On the other hand, the Russian ruble (+1.2%) and the Ukrainian hryvnia (+0.9%) appreciated against the US dollar (Chart 4.25).

Under these conditions, in real terms, the Moldovan leu depreciated by 0.2% against the basket of currencies of the countries – main trading partners of the Republic of Moldova (average of the fourth quarter of 2023 compared to the average of the third quarter of 2023). The largest contributions to the depreciation of the REER were made by Türkiye (-0.5 percentage points) and the Russian Federation (-0.4 percentage points), (Chart 4.27).

In the fourth quarter of 2023 as a whole, the local foreign exchange market remained close to equilibrium, with demand and supply of foreign exchange showing similar trends. However, in November and the last two weeks of the year there was a surplus of foreign currency.

The net supply of foreign currency by individuals amounted to USD 692.8 million, down both in annual terms, by 12.9%, and by 21.2% compared with the previous quarter. The decrease in the supply from individuals was due to the reversal of the trend of individuals' deposit dedollarization and a decline in net transfers from abroad to individuals, which fell by 3.4% compared with the previous quarter and by 19.5% compared with the same period a year earlier, according to data for the first two months of the quarter.

In the structure of the net supply of foreign currency from individuals, the single European currency continued to account for the largest share (71.7%<sup>27</sup>), (Chart 4.28).

The net demand for foreign exchange from the economic agents decreased more sharply, both in annual terms (-22.4%) and compared to the previous quarter (-21.4%), to USD 699.9 million. The widening of the trade balance deficit by 19.6%, according to data for two months of the quarter, was the main factor contributing to the fall in the net demand from legal entities. Compared to the same period of the previous year, there was a decrease in demand for foreign exchange from companies in the energy sector, mainly from the main importer of natural gas and

<sup>27</sup>Share calculated by applying a constant exchange rate.

electricity, but to a lesser extent also from importers of oil products.

The degree of coverage of the net demand for foreign exchange from economic agents by the net supply of foreign exchange from individuals amounted to 99.0% during the reference period (Chart 4.29), compared to 98.7% in the previous quarter and 88.1% in the fourth quarter of 2022. Under these circumstances, the NBM intervened in the domestic foreign exchange market by purchasing foreign exchange in the amount of USD 17.8 million, mainly towards the end of the quarter, when a surplus of foreign exchange was recorded.

In terms of monthly dynamics, the exchange rate of the Moldovan leu against the US dollar remained relatively stable during October, followed by a slight appreciation trend that lasted, with some exceptions, until the end of the quarter. Natural gas import payments continued to be made by the state-owned Energocom company on account of loans obtained from development partners, in particular the European Bank for Reconstruction and Development. Respectively, the absence of this significant component of foreign exchange demand in the heating season conditioned the recording of a foreign exchange surplus during several weeks in November and December. A temporary increase in demand for foreign exchange by some importers of consumer goods in the second week of December caused a short-lived reversal of the exchange rate trend towards depreciation. However, the oversupply of foreign exchange by individuals during the winter holidays caused the MDL/USD exchange rate to resume its appreciating trend.

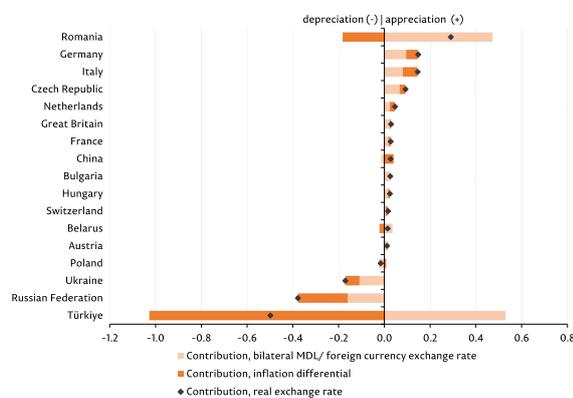
The dynamics of the official exchange rate of the Moldovan leu against the euro was also influenced by the developments of the single European currency against the US dollar on international markets. The development without major fluctuations during October was followed by the upward trend of the EUR/USD exchange rate during November, when the US dollar came under depreciation pressures related to investors' expectations of an earlier start of the rate cutting cycle by the FRS. Labour market, consumption and inflation indicators published during November confirmed the expectations according to which the US interest rates have peaked.

The US dollar continued to lose ground in December when investors' concerns about the sustainability of public debt added to the expectations of monetary policy easing in the US. At the same time, the ECB kept its main monetary policy rates unchanged amid high uncertainty about disinflationary processes and economic growth. Against this background, the euro appreciated by 5.5% against the US dollar compared with the end of the previous quarter.

At the end of 2023, the balance of official reserve assets amounted to USD 5,453.1 million (Chart 4.30), up by USD 571.2 million (+11.7%) compared to the end of the third quarter, mainly due to inflows related to the external financing from development partners.

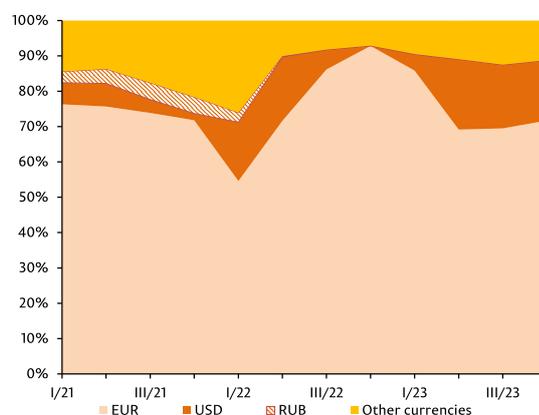
The largest disbursements were recorded from the European Commission in the form of non-reimbursable budget support in the amount of EUR 70 million (equivalent to USD 75.7 million) for

Chart 4.27: Contribution of the main trading partners of the Republic of Moldova to the change in the real effective exchange rate in the fourth quarter of 2023



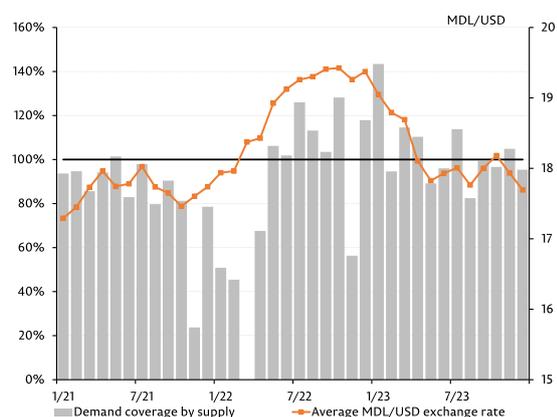
Source: NBM

Chart 4.28: Net supply of foreign exchange from individuals broken down by main currencies (currencies are recalculated in USD at constant average exchange rates)



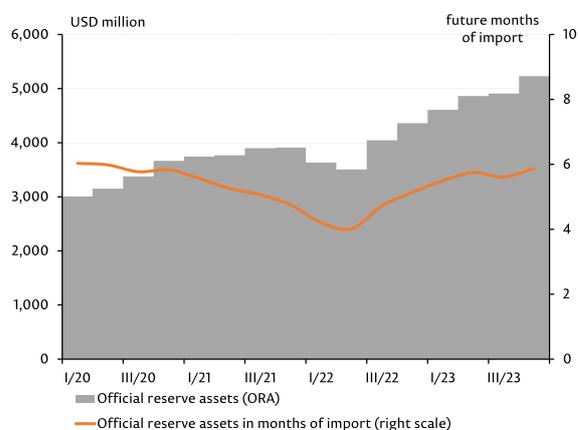
Source: NBM

Chart 4.29: Net sales coverage degree by net supply and exchange rate dynamics



Source: NBM

Chart 4.30: Development of official reserve assets expressed in months of imports of commodities and services (BPM6)



Source: NBM – based on actual data and updated forecast

the energy vulnerability reduction fund, which is intended for compensation payments for energy bills of vulnerable people. In addition, EUR 69.7 million (equivalent to USD 73.9 million) was disbursed under the macro-financial assistance program, including EUR 47.2 million in the form of a loan and EUR 22.5 million in the form of a grant. Another EUR 1.7 million was disbursed to finance various investment projects.

The IMF provided budget support in the amount of SDR 70.95 million (equivalent to USD 94.2 million), the sixth tranche of lending under the Extended Credit and Fund Facilities (ECF/EFF). At the same time, the Japan International Cooperation Agency provided a loan in the amount of JPY 13.5 billion (equivalent to USD 89.8 million) for economic recovery and development, and the French Development Agency provided a loan in the amount of EUR 40 million (equivalent to USD 43.1 million), budget support for the energy sector reform. The World Bank institutions provided loans totaling USD 10.3 million to finance several investment projects, mostly in the education sector. The European Investment Bank disbursed new loan tranches amounting to EUR 3.4 million (equivalent to USD 3.7 million) for the locomotive procurement and rail infrastructure restructuring project.

According to the situation at the end of 2023, official reserve assets continued to provide a sufficient level of coverage of imports of commodities and services (6.1 months of future imports<sup>28</sup>).

<sup>28</sup>Calculated on the basis of the IMF forecast on the import of commodities and services.

## Chapter 5

### Forecast

#### 5.1 External assumptions

**The current round of forecasts assumes that external demand will be weak compared to historical averages and that external inflation will trend towards the levels targeted by monetary authorities. Interest rates in the region and globally will fall, but not as rapidly as previously anticipated. The US dollar will follow a slightly depreciating trend due to low interest rates, the resumption of talks on raising the debt ceiling and the reduced attractiveness of the US dollar. The Russian ruble will fluctuate in the range of USD/RUB 90-100 in line with the new currency realities, which is also the level desired/forecasted by the Russian authorities. Oil prices will be affected by falling consumer demand in China and Europe as well as tensions in the Middle East. Natural gas prices on the international market will be stable, while food prices will increase moderately compared to the previous years' peaks.**

In the table 5.1 are listed the main external assumptions admitted in the Inflation Report, February 2024 forecast round, with their subsequent description.

Economic growth in the euro area is expected to be below potential, with gross domestic product growing by 0.5% in 2024 and 1.3% in 2025. The euro area economy will continue to be affected by the weak performance of the industrial sector, but at the same time, household consumption will be supported by a revival in tourism and rising wages. In 2024, the euro area inflation will fall to the ECB's target of 2.0%, where it will remain in 2025. ECB interest rates will most likely fall, but not as fast and less than previously anticipated, due to concerns about wage growth.

Economic growth in the Russian Federation is expected to moderate from around 2.7% in 2023 to 1.7% in 2024 and 1.3% in 2025. The Russian economy will continue to benefit from high oil prices, appropriate monetary and fiscal policies and the ability to circumvent economic sanctions. At the same time, the cumulative effect of economic sanctions and the lack of structural reforms or public investment will worsen the long-term economic potential. Inflation in the Russian Federation will continue to rise for another two consecutive quarters, after which it will fall towards the Bank of Russia's target of 4.0%. Thus, in the current round of forecasting, average annual inflation in the Russian Federation is expected to be 6.7% in 2024 and 4.7% in 2025. The monetary policy rate will most likely not be raised, and from April 2024 it is expected to be gradually reduced. The Russian ruble will fluctuate in the range of USD/RUB 90-100 according to the new foreign exchange realities, which is also the level desired/forecasted by the Russian authorities.

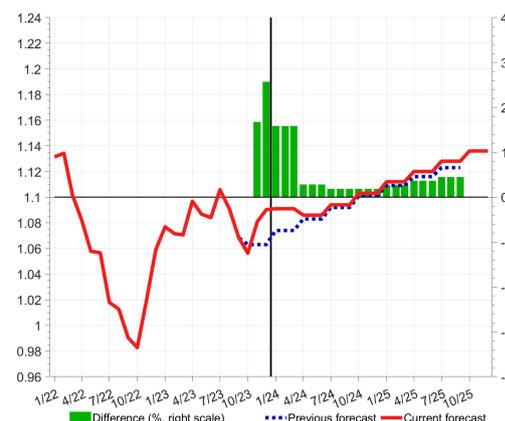
The EUR/USD parity will follow a slightly upward trajectory, with averages for the forecast horizon of 1.09 in 2024 and 1.12 in 2025.

Table 5.1: Expected evolution of external variables (annual average)

	2024	2025
Economic growth in the euro area (%)	0.5	1.3
Economic growth in the Russian Federation (%)	1.7	1.3
Average annual inflation in the euro area (%)	2.2	2.0
Average annual inflation in the Russian Federation (%)	6.7	4.7
EUR/USD	1.09	1.12
USD/RUB	92.7	96.4
Brent oil prices (USD/barrel)	75.5	72.6
International food prices growth (%)	-3.7	3.4

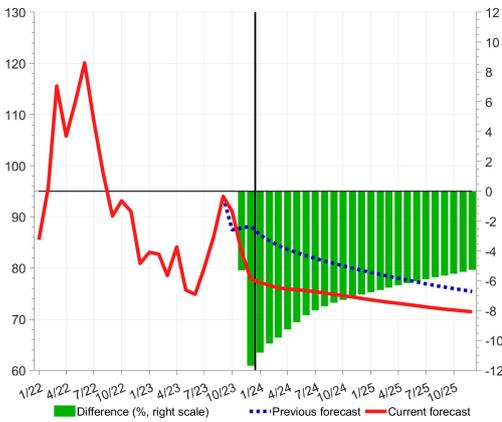
Source: Bloomberg, Consensus Forecast, NBM calculations

Chart 5.1: Exchange rate assumption EUR/USD



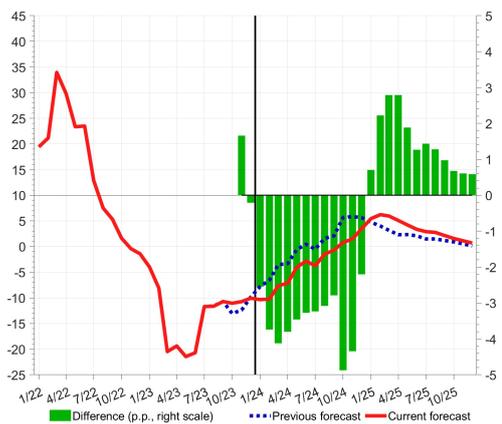
Source: ECB, Consensus Forecast, NBM calculations

Chart 5.2: Brent international oil price assumption (USD/barrel)



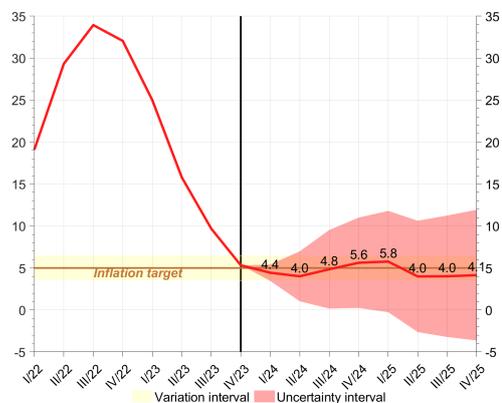
Source: Bloomberg, NBM calculations

Chart 5.3: International food price assumption (%)



Source: FAO, Bloomberg, NBM calculations

Chart 5.4: CPI with uncertainty interval (% compared to the previous year)



Source: NBS, NBM calculations

The forecasts are largely based on the anticipated depreciation of the US dollar due to lower FRS interest rates, possible discussions on raising the debt ceiling and the declining attractiveness of the US dollar amid a lower risk premium. In the recent months, the volatility of the EUR/USD has been quite low, so in the absence of significant shocks, the same low volatility is expected to persist (Chart 5.1).

Oil prices will average USD 75.5/barrel in 2024 and USD 72.6/barrel in 2025 and will be affected by declining consumer demand in China and Europe, even if tensions in the Middle East are a potential upside risk. An important factor will also be the evolution of oil supply from non-OPEC countries, as well as US oil stocks. It should be noted that the external variable related to oil prices on the international market represents the greatest risks and uncertainties in the current round of forecasts (Chart 5.2).

Food prices on the international market will continue to fall from their peaks in 2022 for a little while longer, after which they will slightly increase. Thus, the world food price variable is projected to fall by an average of 3.7% in 2024 and then increase by 3.4% in 2025. Risks are associated with reduced consumer demand, increased logistics and transportation costs, and possible El Niño effects on some agricultural crops. In the region, food import prices from Türkiye could be affected by significant inflation, but also by abundant supplies of cereals from Ukraine (Chart 5.3).

## 5.2 The internal environment

### Inflation

**The annual inflation rate will have a relatively stable trend for the entire forecast period<sup>29</sup>. Inflation will oscillate slightly close to the 5.0% target and will remain within the range throughout the forecast horizon. The minimum value will be recorded in the second quarter of 2024 and in the second and third quarters of 2025, and the maximum value in the first quarter of 2025** (Chart 5.4).

The positive rate of inflation will be due to the favorable impact from *core inflation*, *regulated prices*, *food prices* and less from *fuel prices*, except in the first, third and fourth quarters of 2024, when fuel prices will have a slightly negative impact (Chart 5.5).

The presence of factors such as, (1) significantly disinflationary internal demand over the entire forecast horizon, (2) disinflationary pressures from domestic products on the backdrop of the rich harvest in 2023, (3) continued decline in oil prices in the international market over the entire forecast horizon, (4) the previous year’s high base, (5) the anticipated moderate decline in natural gas prices, except in the fourth quarter of 2024 and the first and fourth quarters of 2025, and (6) the moderation in imported inflation in the second quarter of 2024 and for three consecutive quarters beginning in the first quarter of 2025 will cause the annual inflation rate to decline.

<sup>29</sup>First quarter of 2024 – fourth quarter of 2025

However, (1) the accumulated increases in energy resource prices internationally, (2) the adjustment of excise taxes in early 2024 and 2025, (3) the second-round effects in the first half of this year from rising food prices on core inflation, (4) the slight upward trend in food prices on the international market over the entire forecast horizon, except for the first quarter of 2024 and the third quarter of 2025, (5) the anticipated moderate increase in natural gas prices starting in the fourth quarter of 2024 for two consecutive quarters and the fourth quarter of 2025 will dampen the decline in the annual rate and contribute to its slight acceleration.

The annual inflation rate, for the forecast period, will record the minimum value of 4.0% in the second quarter of 2024 and the second and third quarters of 2025 and the maximum value of 5.8% in the first quarter of 2025.

Average annual inflation will be 4.7% and 4.5% this year and next year, respectively.

**The annual rate of core inflation will increase only slightly in the first half of this year, after which it will decline slightly until the end of the forecast horizon<sup>30</sup>, except for the last quarter of the forecast, when it will slightly increase** (Chart 5.6).

The downward trajectory of core inflation will be driven by (1) significantly disinflationary internal demand over the entire forecast horizon, (2) the high base from the previous year except for the fourth quarter of 2023 and (3) continued moderation in imported inflation exception for the first quarter of 2024.

However, (1) the adjustment of excise taxes in early 2024 and 2025, (2) the increase in imported inflation in the first quarter of 2024, (3) second-round effects in the first half of this year from the food prices increase will dampen the decline in the annual rate and help accelerate it during the first semester of 2024 and the fourth quarter of 2025.

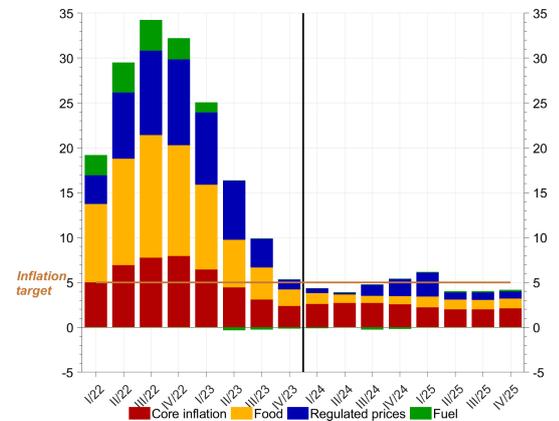
Average annual core inflation rate will be 6.4% and 5.1% in 2024 and 2025, respectively.

**The annual food price inflation rate will trend slightly downward for the beginning of the forecast horizon, after which it will trend relatively steady until the end of the forecast period** (Chart 5.7).

The downward trajectory of the annual rate of food prices will be influenced by (1) negative internal demand over the entire forecast horizon, (2) disinflationary pressures from domestic products on the backdrop of the rich harvest in 2023, (3) high base, (4) negative rate of imported inflation for the first two consecutive quarters of the current year.

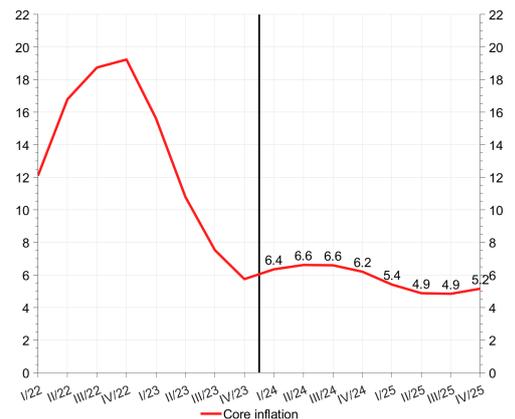
The positive rate of imported inflation from the second half of the current year through the end of the forecast period and (2) the slight upward trend in food prices on the international market over the entire forecast horizon, except for the first quarter of 2024 and the third quarter of 2025, will dampen the decline in the annual rate.

Chart 5.5: CPI decomposition (% , percentage points, compared to the previous year)



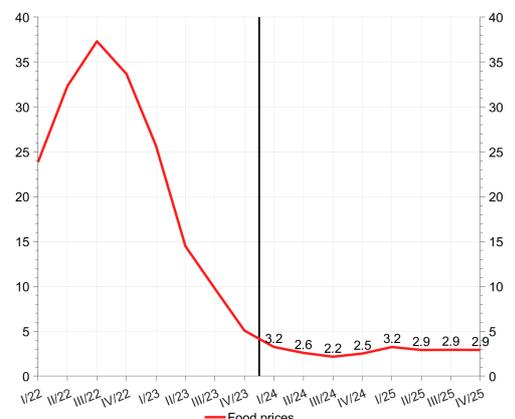
Source: NBS, NBM calculations

Chart 5.6: Core inflation (% , compared to the previous year)



Source: NBS, NBM calculations

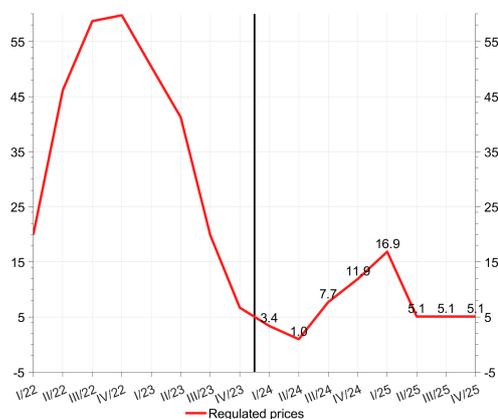
Chart 5.7: Food prices (% , compared to the previous year)



Source: NBS, NBM calculations

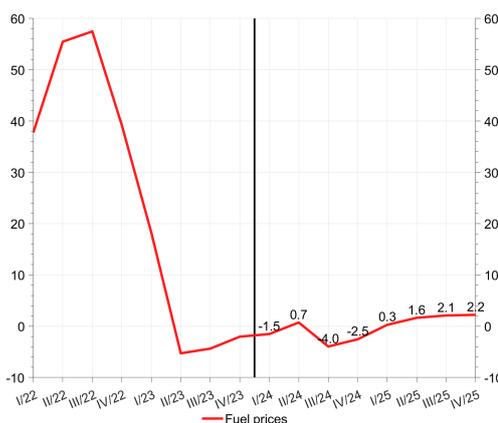
<sup>30</sup>Fourth quarter of 2025

Chart 5.8: Regulated prices (% , compared to the previous year)



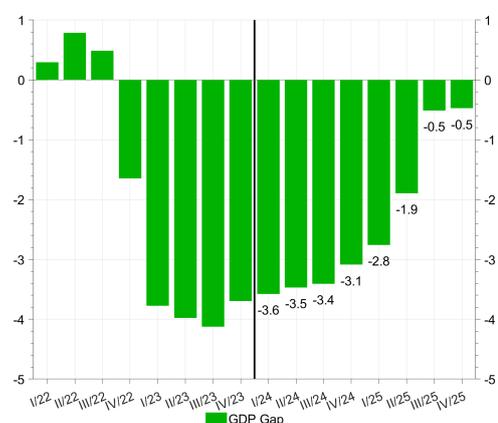
Source: NBS, NBM calculations

Chart 5.9: Fuel prices (% , compared to the previous year)



Source: NBS, NBM calculations

Chart 5.10: GDP deviation (%)



Source: NBM calculations

The average annual rate of food prices will be 2.6% and 3.0% in 2024 and 2025, respectively.

**The annual rate of regulated prices will decline in the first half of the current year, then increase rapidly until the first quarter of 2025, after which it will decline in the following quarter and remain stable until the end of the forecast horizon** (Chart 5.8).

The annual rate will be determined by the recent and anticipated adjustments in the first half of the current year and the first quarter of 2025 to a number of tariffs.

The increase in costs, in particular for energy and wages, on the one hand, and, on the other hand, the non-adjustment or insufficient adjustment of tariffs for these services over long periods, sometimes years, are the main factors behind the high rates of regulated prices. The decrease in the annual rate of regulated prices in the first half of this year and in the second quarter of 2025 will be due to the expected moderate decline in external energy prices, but also to the effect of the high annual base.

The average annual rate of regulated prices will be 5.9% and 7.8% in 2024 and 2025, respectively.

**The annual rate of fuel prices will slightly increase, at modest rates, until the end of the forecast horizon, except in the third quarter of 2024** (Chart 5.9).

The upward trend in fuel prices is due to (1) the adjustment of excise taxes in early 2024 and 2025, (2) the low base in the previous year, except for the first quarter of 2023, and (3) a slight increase in imported inflation in the fourth quarter of 2024.

However, (1) negative internal demand and (2) declining oil prices on the international market over the entire forecast horizon will dampen the increase in the annual rate and contribute to a slight decline in the third quarter of 2024.

Annual average rate of fuel prices will be -1.8% and 1.6% in 2024 and 2025, respectively.

## Demand

**Aggregate demand will be negative for the entire forecast period due to deteriorating external demand and modest financing of household consumption, as well as tightening monetary conditions. The rich agricultural harvest in the previous year and the positive fiscal impulse as from the second quarter of 2025 for two consecutive quarters will dampen the decline in aggregate demand** (Chart 5.10).

The deterioration in external demand, (2) the decline in real terms of remittances for 2024, (3) the slightly restrictive effects of real monetary conditions will be the main factors that will act down aggregate demand.

The previous year's rich agricultural harvest, (2) the revival of household consumption financing sources in real terms, (3) the positive fiscal impulse as from the second quarter of 2025 for two

consecutive quarters, the recovering external demand, though negative, will mitigate the fall in aggregate demand and will lead to a recovery in aggregate demand.

The real effective exchange rate deviation, although declining, will continue to be restrictive on aggregate demand. On the other hand, the real interest rate will stimulate internal demand throughout the forecast horizon. External demand from both eastern and western economic partners will have a negative impact on internal demand.

**Monetary policy**

**Real monetary conditions will be restrictive, albeit diminishing, on aggregate demand for the entire forecast period** (Chart 5.11).

Monetary policy through the real effective exchange rate will be restrictive and through the real interest rate stimulative over the forecast horizon.

The real depreciation of the national currency has significantly reduced the deviation of the real effective exchange rate from its equilibrium level, thereby considerably diminishing the restrictive effects on aggregate demand in the first quarter of the forecast. Over the forecast horizon, a decreasing trend in the restrictiveness of the real effective exchange rate deviation is anticipated.

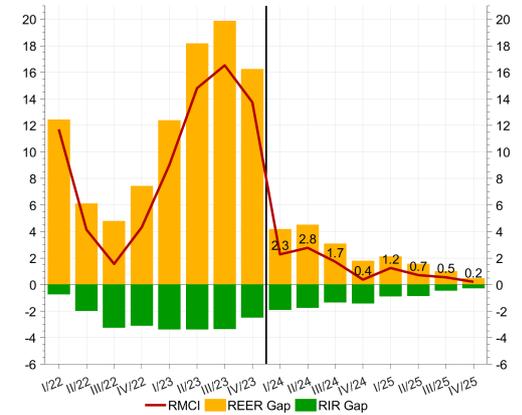
**5.3 Comparison of forecasts**

**Current inflation forecast compared to that in the previous inflation report<sup>31</sup>, have been revised insignificantly downward in the first quarter of 2024 and upward for the remainder of the comparable period<sup>32</sup>** (Chart 5.12).

The upward revision of the forecast of regulated prices over the entire comparable period, excluding the first quarter of 2024, and of core inflation will lead to an upward revision of the current forecast of the annual inflation rate. However, the decrease for the whole comparable period in the forecast of food prices, regulated prices in the first quarter of 2024, and fuel prices for the whole comparable period will revise downward the current forecast of the annual inflation rate (Chart 5.13).

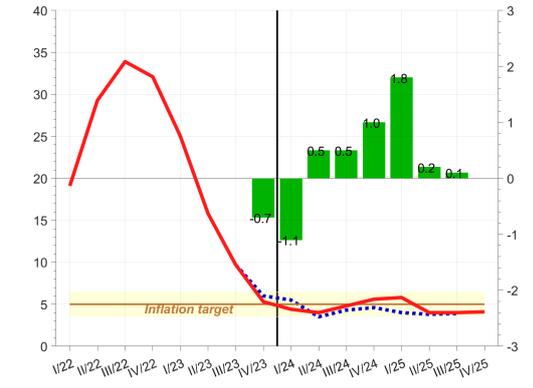
The higher projection of the annual inflation rate forecast is driven by (1) the anticipation of tariff increases in the first quarter of 2024, (2) the effect following the previous quarter's increase in the water and sewerage tariff, (3) the anticipation of less restrictive aggregate demand over the comparable period, (4) higher than anticipated actual inflation and a higher than anticipated short-term forecast of core inflation, largely as a result of adverse sectoral shocks in the previous quarter, (5) the re-estimate of the impact of reflecting the effect of the finalization of the period of

Chart 5.11: Real monetary conditions index and decomposition



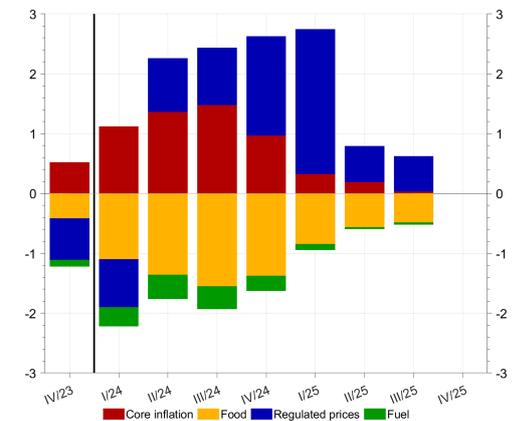
Source: NBM calculations

Chart 5.12: CPI (%), compared to the previous year, percentage points



Source: NBS, NBM calculations

Chart 5.13: Decomposition of the difference between forecasts (percentage points)



Source: NBM calculations

<sup>31</sup>Inflation Report, November 2023

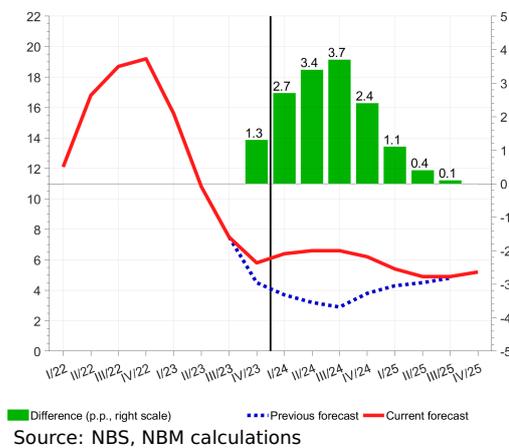
<sup>32</sup>First quarter of 2024 – third quarter of 2025

state compensation of energy resource prices in the cold period of the year for the 2023-2024 season, (6) a higher-than-anticipated import price of natural gas in the first quarter of 2024, (7) a higher imported inflation trajectory from the fourth quarter of 2024 through the end of the comparable period, and (8) the anticipation of tariff increases in the first quarter of 2025.

However, (1) lower actual inflation than anticipated in the previous quarter, (2) a significantly downward-looking short-term forecast, (3) lower projected international food prices over the entire comparable period, (4) a lower trajectory for imported inflation starting in the first quarter of 2024 for three consecutive quarters, (5) a significantly lower forecast for international oil prices and the import price of natural gas except in the first quarter of 2024, (6) reconsideration of the seasonal effect from the cold part of the year, (7) exclusion of the adjustment for excise taxes on food products, and (8) the re-estimation of the impact of strong seasonality in the second and third quarters of 2024 and 2025 dampened the upward revision to the current forecast and led to the downward revision in the first quarter of 2024.

The average annual inflation rate was increased by 0.2 percentage points for 2024 and by 0.5 percentage points for 2025.

Chart 5.14: Core inflation (% , compared to the previous year, percentage points)

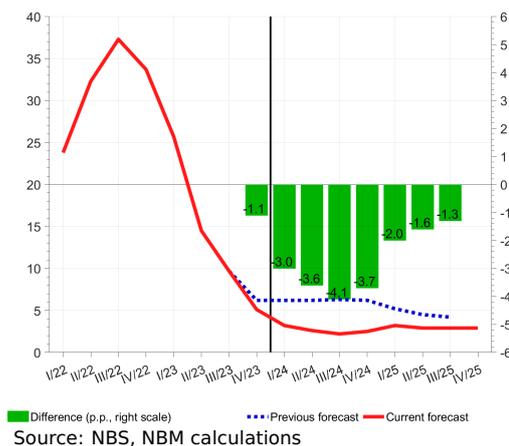


**The current forecast for the annual rate of core inflation has been revised significantly upwards over the entire comparable period** (Chart 5.14).

The higher projection of the current forecast relative to the previous one is driven by (1) higher actual inflation than anticipated in the previous quarter, as a result of adverse sectoral shocks, (2) a significantly upward short-term forecast, (3) a higher imported inflation trajectory, and (4) expectations of less restrictive aggregate demand over the entire comparable period, but also (5) a slightly higher adjustment in excise taxes. Reconsideration of the seasonality effect from the cold period in the fourth quarter of 2024 has dampened the upward revision to the current forecast.

The forecast for the average core inflation rate has been increased by 3.0 percentage points for 2024 and by 0.4 percentage points for 2025.

Chart 5.15: Food prices (% , compared to the previous year, percentage points)



**The annual rate of food prices has been revised downwards over the entire comparable period** (Chart 5.15).

The lower rate of the current forecast relative to the previous one is driven by (1) a declining short-term forecast, (2) lower actual inflation than previously anticipated, (3) lower food prices on the international market over the whole comparable period, (4) lower imported inflation as from the first quarter of 2024 for three consecutive quarters, (5) re-estimating the seasonal effect in the cold period of the year, namely in the fourth quarter of 2024 and 2025, (6) excluding the excise tax adjustment, but also (7) re-estimating the impact of highly seasonal products in the second and third quarters of 2024 and 2025.

The anticipation of a (1) less restrictive aggregate demand over the entire comparable period and (2) a higher imported inflation from the fourth quarter of 2024 through the end of the comparable



## 5.4 Risks and uncertainties

### External sector

- ***The impact on energy resource prices in the event of heightened tensions in the Middle East.*** As of October 2023, geopolitical tensions in the Middle East have intensified, but there has been no impact on production or transportation capacities for oil or other energy resources. Therefore, since the peak levels reached in October 2023, oil and natural gas prices have followed a slightly downward trajectory, which initially seemed counterintuitive. However, this risk still persists and the possible effects on energy resource prices will be significant (proinflationary).
- ***Blocking access to Red Sea transportation for a longer period.*** Beginning in December 2023, Houthi rebels in Yemen attacked several merchant ships crossing the Red Sea, and in early 2024, the USA and allies retaliated on their bases in Yemen. This caused merchant ships to be redirected to circumnavigate the African continent, which increased the delivery time of transported goods and increased logistics and transportation costs. Already, some automotive industry plants in Europe have announced they are suspending operations for a few weeks to wait for the parts needed for the assembly-line production process. Although raw material or finished product prices have not currently shown a prompt reaction to the situation, several industry experts warn that if the situation persists, production and consumer prices will be hit imminently by rising transportation costs (proinflationary).
- ***Continuation of the war in Ukraine.*** The war in Ukraine continues, making it difficult to anticipate possible shocks and long-term effects on the regional and local economy. The immediate proximity of the armed conflict decreases the volume of investment and increases the pressure on consumer price formation due to existing risks (proinflationary).
- ***Increase in consumer prices in Türkiye and the Russian Federation.*** Currently, both the Russian Federation and Türkiye are facing increasing proinflationary pressures that could affect the prices of Moldovan importers, if we disregard the real effective exchange rate. At the same time, the vacation packages in Türkiye will be more expensive for the Moldovan population, which will reduce their disposable income or could lead to a redistribution of personal expenditure (proinflationary).
- ***Temporary supply shocks on international food price formation.*** Although global food supply and demand are currently fairly balanced, shocks such as the El Niño effect on some agricultural crops, poor agrometeorological conditions, transportation bottlenecks or export restrictions could affect the global prices for agricultural products (proinflationary).

- **Continued sharp moderation in the rate of economic activity in the euro area.** Statistical data on industrial production and economic activity show that in the second half of 2023, European economies were in a sharp decline. The primary and secondary consequences of the 2022 energy crisis and rising interest rates affected both demand and supply. If monetary stimulus from the ECB is delayed, external demand is weak, or the electoral period in the EU affects fiscal policies and public investment, economic growth in the euro area will continue to be below potential (disinflationary).
- **Uncertainties related to the transition period from tighter monetary conditions to lower interest rates.** At the last monetary policy meetings the FRS and the ECB maintained interest rates and signaled the end of the period of monetary tightening. The uncertainties now relate to the timing and magnitude of the cut in interest rates. While the US economy is performing relatively well and the FRS has room to maneuver, growth in the euro area is below potential and the ECB is concerned about proinflationary pressures related to wage growth (uncertainty).
- **Geopolitical configuration after the 2024 elections.** Globally, more voters than ever before in history will head to the polls in 2024, as at least 64 countries plus the European Union, representing about 49% of the world's population, are set to hold electoral elections, the results of which, for many countries, will prove decisive for years to come<sup>33</sup> (uncertainty).

## Real sector

- **Uncertainties about the timing and magnitude of the adjustment of regulated tariffs.** The medium-term inflation forecast is based on a trajectory for prices of regulated services that is consistent with certain assumptions about international and regional energy prices and other indicators relevant to the sector. However, given that tariffs for some regulated services have a considerable economic impact on the population, the timing of their adjustment may be driven not only by economic factors, but also by the pursuit of social or political objectives by the decision-makers involved. Therefore, the timing and magnitude of tariff adjustments cannot be estimated with sufficient confidence (uncertainty).
- **Uncertainties on how the NBS reflects the compensation for energy resources.** The current tariffs for natural gas, heat and electricity were taken into account in the medium-term inflation forecast. However, the previous cold season as well as the data published by the NBS for November and December 2023 showed that the trajectory of regulated prices may oscillate significantly from that forecasted depending on how the compensation for energy resources granted to the population during the cold season is reflected. Therefore, the trajectory of regulated prices could be different from the assumed one depending on how the NBS will reflect these compensations in the CPI (uncertainty).

<sup>33</sup><https://time.com/6550920/world-elections-2024/>

- **Regional natural gas price decrease and possible domestic tariff adjustment.** The decrease in natural gas prices in the region in the previous year and at the beginning of the current year would create preconditions for decreasing the tariff for network gas and thermal energy once the financial deviations accumulated in the previous periods are covered. However, in view of the possibility of gas reserves procured at a relatively higher price, as well as the tariff deviations accumulated in the previous periods, the decrease in the tariff may be delayed. Once the previously accumulated financial deviations disappear, there will be preconditions for reducing the tariff for the network gas in the following period, which will imply a reduction in the thermal energy tariff as well. However, the exact timing and magnitude of the adjustments is uncertain (uncertainty, disinflationary).
- **Decrease in the number of consumers on the territory of the Republic of Moldova.** The military conflict in Ukraine has caused massive population outflows from Ukraine. Some of the refugees are in the Republic of Moldova, directly contributing to the increase in consumption. Their return to their country of origin or their departure to other regions would lead to a lower demand on the domestic market (uncertainty, disinflationary).
- **Vulnerability of prices of domestic fruits and vegetables to weather conditions in the coming period.** According to the experience in recent years, the prices of domestic fruit and vegetables are largely affected by adverse weather conditions such as frosts, heavy rainfall, costs associated with harvesting, transportation, storage, but also their marketing at marketing outlets in the country. In case of occurrence of lower than normal temperatures, such as in the spring of 2023, or heavy rainfall, this would result in higher than forecasted food prices in the next period (proinflationary).
- **Uncertainties about the agricultural production in 2024 and 2025.** This year's and next year's agricultural harvest and domestic food prices, respectively, will depend, for the most part, on the agrometeorological conditions in that period. In this way, developments in the agricultural sector and, consequently, the trajectory of food prices for the years 2024 and 2025 continue to be marked by uncertainty. If the agricultural harvest is jeopardized (dry conditions, late frosts), the GDP growth rate for the current year will be lower than anticipated. A smaller agricultural harvest will generate higher inflationary pressures on food prices (uncertainty).
- **The escalation of the military conflict in the Middle East will support the increase in the prices of energy resources, but also of other CPI products.** The increase in international and regional oil prices will lead to higher motor fuel prices on the domestic market and will create the preconditions for higher prices for other energy resources and the adjustment of some tariffs locally. At the same time, the maintenance or escalation of tensions in the region will support increases in transportation expenditures and, as a result, final prices for other goods (proinflationary).

## Monetary and public sectors

- **Evolution of the NEER/REER effective exchange rate.** The appreciation in nominal and real effective terms of the national currency is a stimulus on imports and has the potential to affect Moldova's net exports. Combined with the recent increase in prices of goods and services on the international market, the trade balance deficit will keep a negative trend, fueling the depreciation pressures on the Moldovan leu (proinflationary).
- **Monetary transmission mechanism.** The change in monetary conditions propagates slowly on the rates of new loans granted in MDL, this leads to the procrastination of decision making by economic agents and households on taking new loans. At the moment, the transmission channels of monetary policy actions, i.e. the interest rate channel and the credit channel, are functioning poorly, leading to the spread over time of the effects of monetary policy actions on the national economy (disinflationary).
- **Banking sector liquidity.** Since an excess of foreign exchange was created on the foreign exchange market, the NBM intervened by purchasing foreign exchange, thus, an additional volume of liquidity in MDL was released on the money market. At the same time, following the decisions to lower the base rate and, as a consequence, the lower interest rates on term deposits in MDL, the balances of these deposits also decreased, leading to a reduction in liquidity in the banking system. However, this surplus remains sizable and may have a positive short-term impact on aggregate demand, the exchange rate and may generate inflationary pressures. At the same time, in the medium term, following a change in the trend on the foreign exchange market and a continuation of the downward trend on the interest rate market, this excess liquidity will be significantly reduced, with a direct impact on credit resources, generating disinflationary pressures (uncertainty).
- **External funding.** Increased flow of external loans and grants allow for faster implementation of reforms in the domestic economy and create additional stimulus on inflation. Estimates point, in the medium term, to a decline in the financing of the state budget balance from external sources, due to a reduction in the flows to support the budget. Thus, it is planned to allocate external sources mainly for the implementation of capital investment projects. External funding will stimulate the continued growth of excess liquidity in the banking system, which will have a positive impact on aggregate demand, the exchange rate of the national currency and generate additional inflationary pressures. At the same time, the degree of realization of externally financed projects remains low, implying that the disbursement of funds for the development of various sectors of the national economy is delayed (uncertainty).
- **Dollarization of deposits.** The maturity of the "expensive" deposits attracted last year and the trend of a continuous decrease in the rates on new deposits attracted in national currency, which are closer and closer to the rates on deposits attracted in foreign currency, create the premises for an

increase in the dollarization of deposits, a phenomenon observed over the last seven months. This stimulates the demand for foreign currency, creating depreciation pressures on the exchange rate, while generating inflationary pressures in the future periods (proinflationary).

- **Compensation for gas, thermal energy and electricity tariffs.** In the context of the current energy crisis and the increase in prices and tariffs for gas, thermal energy, electricity, the Government has developed the mechanism for compensating vulnerable consumers. Thus, the state will implement a specific form of social protection targeted at vulnerable consumers against economic poverty. The implementation of the compensation mechanism will require additional financial means from the state budget (granted from December 2023 to April 2024) (proinflationary).
- **Budget financing and fiscal impulse.** In the context of the recent crises, public finances are subject to significant pressures, stemming primarily from the mitigation of the impact of these crises on the population and economic agents. The budgetary projections for the next year are based on the assumption of a declining budget deficit and, at the same time, more modest financing from external and internal sources. The government will have to strengthen its efforts to ensure the sustainability of public finances while safeguarding the execution of budgetary obligations in the social area. The risk to the financing of the state budget could result in insufficient fiscal impulse to revive the economy more rapidly and mitigate the consequences of the recent crises (disinflationary).

## Chapter 6

# Monetary policy decisions

### Summary

#### of the meeting of the Executive Board of the National Bank of Moldova from 20.06.2023 on the promotion of monetary policy

**The meeting was chaired by:** Mr. Octavian Armasu, Governor – Chairman of the Executive Board

**Attendees:** Executive Board members – Mr. Vladimir Munteanu, First Deputy Governor – Deputy Chairman of the Executive Board, Mr. Arcadie Albul – Deputy Governor, Mrs. Tatiana Ivanicichina – Deputy Governor, Mr. Constantin Schendra – Deputy Governor

**Rapporteur:** Mr. Octavian Teaca – Deputy Director of the Monetary Policy Department, Head of the Macroeconomic Analysis and Forecasting Department

**Guests:** Mr. Natan Garstea, Mrs. Natalia Sirbu – Advisers to the Governor, Mr. Daniel Savin – Director of the Financial Markets Department, Mrs. Valentina Rusu – Director of the Legal Department, Mrs. Alina Boboc – Head of the Financial Education and Communication Department

The meeting of the Executive Board of the NBM on the promotion of monetary policy started with the presentation of the Report assessing the risk of inflation forecast deviation carried out by Mr. Octavian Teaca. It was emphasized that this report was prepared on the basis of information and analysis from the external and internal environment available after the April 2023 forecasting round. At the same time, the trends of the main macroeconomic indicators were specified, identifying the risks and uncertainties that are likely to affect the short and medium-term inflation forecast in the Inflation Report, May 2023.

The EB members assessed and analyzed the information on macroeconomic developments available since the April forecast and most members noted the confirmation of the validity of the inflation forecast prepared and presented in the Inflation Report, May 2023. At the same time, it was noted that the updated information signaled the persistence of the risk of a slightly downward deviation of the inflation forecast.

In the discussions associated with the developments of domestic inflation, the EB members noted that the annual inflation rate in May 2023 continued its downward trajectory, registering 16.3% and being 0.6 percentage points above the anticipated level. The EB members noted that the deviation of actual inflation from the forecast is mainly driven by the positive impact of regulated prices and food prices, which increased by 46.1% and 14.0%, respectively, in annual terms, being 2.3 and 0.9 percentage points above the levels anticipated in the Inflation Report, May 2023.

Assessing the determinants of the respective development, it was emphasized that the dynamics of regulated prices was caused by the increase in air passenger transport prices for international flights and the reflection of the partial effect of the electricity tariff adjustment in April 2023, while food prices were caused by the more pronounced dynamics of volatile prices.

It was also noted that pressures from core inflation were dampened by the gradual dissipation of second-round effects associated with gas and electricity tariffs from previous periods, together with the persistence of disinflationary aggregate demand and exchange rate appreciation. Thus, core inflation in May 2023 was 0.1 percentage points lower than the forecast value, constituting 10.5%. Fuel prices (-3.4%) were supported by the lower-than-expected trajectory of oil prices and a more appreciating exchange rate, being 0.6 percentage points below the forecast value.

Estimating the inflation outlook, it was emphasized that although annual inflation in April-May 2023 was marginally higher than forecast, the earlier than anticipated decline in natural gas tariffs, together with the more modest dynamics of oil prices, point to a similar trajectory for the annual inflation rate for the second quarter of

2023 as projected in the Inflation Report, May 2023.

Analyzing global economic conditions, it was cautioned that they remain under pressure from subdued demand, along with the looming risks and uncertainties associated with the war in Ukraine. From the perspective of tempered global demand, it was noted that oil, food, and raw material prices on the international market have declined, and against this backdrop global inflation has moderated, but remains well above the pre-pandemic levels.

During the discussions associated with the national economic conditions, the EB members noted that the Moldovan economy continued to register negative growth rates in the first quarter of 2023, but of a more subdued magnitude compared to the last two quarters of the previous year. Thus, gross domestic product contracted by 2.4% in real terms in the first quarter of 2023 compared to the same period of the previous year, generating disinflationary pressures from aggregate demand during that period.

In this context, it was noted that the development of the growth rate of economic activity was supported by the dynamics of household consumption, which reversed its downward trend, recording a decrease of 2.6%, amid the decline in real terms of disposable income of the population and the still restrictive credit conditions. Gross fixed capital formation (-0.4%), together with net exports of goods and services, had a negative impact on the GDP development. At the same time, the contraction in economic activity was driven by negative developments in industry, trade and construction. Gross value added in agriculture contracted by 4.0% in the first quarter of 2023.

From the perspective of consumption financing sources, it was noted that the wage fund in real terms decreased by about 3.9% in the first quarter of 2023 compared to the same period of the previous year. On the other hand, money transfers in March 2023 maintained the positive dynamics of the first two months of this year, registering 15.3%.

Thereafter, the members of the EB commented on the monetary conditions, noting that the gradual stimulative monetary policy stance through the interest rate channel adopted since the end of last year, together with the money market conditions, have conditioned the reduction in interest rates on new loans and new deposits attracted in national currency during the period February-May 2023.

After analyzing the statistical data associated with money market, the weighted average interest rate on new loans granted in MDL decreased by 0.27 percentage points in May this month, reaching the level of 13.36% annually, while the weighted average interest rate on new term deposits in MDL recorded the level of 8.36% annually, being 0.19 percentage points lower than in April 2023. In this context, it was underlined that the development of rates favored the dynamics of the volume of new loans granted in MDL, which increased by 9.3% in May compared to the previous month.

Guided by the available macroeconomic information analysis and assessment, after the preparation of the April forecast round, the EB members agreed that the development of the medium-term inflation forecast was projected slightly downward over the forecast horizon. At the same time, the expectation of a slightly higher forecast for international food prices from 2024 onwards mitigated the slightly negative deviation.

Among the deviation risks to the April 2023 inflation forecast were a more appreciating exchange rate trend, a lower domestic demand forecast, and more subdued import prices for natural gas and oil on the international market.

The EB members also emphasized that the tense situation in the region and potential escalations, the volatility of energy prices at the regional level, the way of adjusting tariffs for utilities (natural gas, thermal energy and electricity) maintain uncertainty about the inflation outlook in the short- and medium-term. The relevance of the uncertainty regarding agricultural production in the current and next year was also noted.

During the deliberations on the draft decision on the monetary policy measures proposed by the Monetary Policy Department, the EB members' views were divided. Some of the EB members were concerned about money market conditions, in particular the excessive liquidity in the banking sector, which could hamper the transmission of monetary policy and pose short- and medium-term risks to inflation.

At the same time, there was also concern about the possible approximation of the monetary policy rate of the National Bank of Moldova with the monetary policy rate of the European Central Bank (ECB).

Following the analyses and findings made during the meeting, the majority of the members of the Executive Board of the NBM noted the confirmation of the assumptions and conclusions considered in the April 2023 forecast and the downward trend of the annual inflation rate under the impact of the strong disinflationary pressures from internal and external demand, thus justifying the maintenance of the stimulative monetary policy. Thus, by a majority vote, the Executive Board decided to lower the base rate and the rates on the standing facilities by 4.0 percentage points.

In this regard, it was noted that this decision continues the series of stimulus measures adopted by the NBM

in the recent period and aims to create the monetary conditions necessary to bring inflation within the range of  $\pm 1.5$  percentage points of the inflation target of 5.0% and to maintain it within this range in the medium-term.

The EB members also emphasized that the NBM's decision is aimed at supporting the balance of the national economy by creating monetary conditions for boosting credit in the context of lowering related costs, reviving consumption, thus contributing to boost the aggregate demand.

At the end of the meeting, it was emphasized that further decisions of the Executive Board will depend on the dynamics and medium-term outlook for inflation, monitoring and assessing risks in the internal and external environment.

**Decision adopted by the Executive Board of the NBM by majority vote:**

- 1. The base rate applied to the main short-term monetary policy operations is set at 6.00% annually.**
- 2. Interest rates are set:**
  - a) on overnight loans, at the level of 8.00% annually;**
  - b) on overnight deposits, at the level of 4.00% annually;**
- 3. The required reserve ratio from the funds attracted in MDL and non-convertible currency is maintained at the current level of 34.0% of the calculation base.**
- 4. The required reserve ratio from the funds attracted in freely convertible currency is maintained at the current level of 45.0% of the calculation base.**

**Voting results of the EB members**

FOR – 3

AGAINST – 2

**Chairman of the Executive Board**

**Secretary of the Executive Board**

**Octavian ARMASU**

**Sergiu SURDU**

**Summary**  
**of the meeting of the Executive Board of the National Bank of Moldova from 09.08.2023**  
**on the promotion of monetary policy**

**The meeting was chaired by:** Mr. Octavian Armasu, Governor – Chairman of the Executive Board

**Attendees:** Executive Board members – Mr. Vladimir Munteanu, First Deputy Governor – Deputy Chairman of the Executive Board, Mrs. Tatiana Ivanicichina – Deputy Governor, Mr. Arcadie Albul – Deputy Governor

**Rapporteur:** Mr. Radu Cuhal – Director of the Monetary Policy Department

**Guests:** Mr. Alexandru Savva, Mrs. Natalia Sirbu – advisers to the Governor, Mr. Daniel Savin – Director of the Financial Markets Department, Mrs. Valentina Rusu – Director of the Legal Department, Mrs. Alina Boboc – Head of the Financial Education and Communication Department

After the opening of the Executive Board meeting on the promotion of monetary policy, the floor was given to Mr. Radu Cuhal, who presented the comprehensive analysis of the recent phenomena and developments in the external and internal environment, trends and prospects of the main macroeconomic indicators included in the Inflation Report, August 2023. At the same time, the new scenarios related to the inflation forecast round for the next eight quarters, the associated assumptions and hypotheses, along with the risks and uncertainties identified at the time of the preparation of the report were presented.

The EB members noted that recent macroeconomic information confirms the veracity of the latest NBM forecast. At the same time, it was emphasized that the timely adoption of restrictive monetary policy measures during 2022 led to a change in the inflation trend. Thus, it was noted that after the peak value reached in October 2022 (34.6%), the inflationary process reversed, with inflation reaching 13.2% in June 2023.

It was noted that annual actual inflation in the second quarter of 2023 was 0.2 percentage points above the forecast value, the deviation being mainly caused by food prices due to the higher than expected increase in fruit and potato prices as a consequence of the weather conditions in the spring of this year.

The factors keeping inflation above the upper end of the  $\pm 1.5$  percentage point range from the 5.0% target were discussed, highlighting the tariff hikes with their spillovers, the war in Ukraine, last summer's drought, the excise tax hike at the beginning of the year, and the cooler weather in spring 2023. It noted that the disinflationary demand since mid-2022 and the appreciation of the MDL since the beginning of this year continue to ease some of the pressures from the aforementioned factors.

Analyzing the external macroeconomic situation, the global economy continued its post-pandemic recovery at a slow and fragmented pace. Thus, the tightening of monetary policies in major economies has dampened global demand and thus raw material prices. Although inflation rates are approaching target levels, monetary authorities are cautious in changing the monetary policy cycle.

It was also noted that Saudi Arabia and the Russian Federation have announced further cuts in oil supply, but weak demand, especially from China, and sufficient oil supply from non-OPEC countries have halted the rise in market prices. Natural gas prices in Europe reached pre-energy crisis levels and food prices on the international market continued to fall, with the exception of sugar and cereal prices.

The discussion then centered on domestic economic conditions and it was noted that economic activity declined sharply at the beginning of this year, with the annual real GDP growth rate being negative of 2.4% in the first quarter of 2023. It was noted that this was driven by subdued domestic demand as a result of declining population's real incomes and tighter credit conditions, rising energy prices and heightened uncertainty in the region. On the demand side, public administration consumption and investment rose, while population consumption, exports and imports fell. On the supply side, agriculture, industry, trade and construction contracted, while the health and social care, real estate transactions and information and communication sectors developed positively.

During the meeting, Mr. Radu Cuhal presented the development of monetary conditions, noting that the weighted average interest rates on new loans in national currency and on term deposits have recorded reductions in the second quarter of 2023 compared to the previous quarter under the impact of the transmission mechanism of the consecutive rate cuts applied to the main monetary policy operations started in December 2022. In this

regard, it was emphasized that the weighted average interest rate on deposits in MDL recorded 7.29% in the second quarter of 2023, decreasing by 4.47 percentage points compared to the previous quarter. In the second quarter of 2023, the weighted average interest rate on new loans in domestic currency amounted to 13.18% annually, lower by 1.11 percentage points than in the first quarter of 2023. In this context, further decline in lending interest rates is anticipated. At the same time, it was revealed that the excess liquidity in the second quarter of 2023 amounted to MDL 14.4 billion, increasing by MDL 2.6 billion compared to the first quarter of 2023.

In the discussions that followed, the EB members referred to the current inflation forecast, noting that, according to it, the annual inflation rate in the third quarter of 2023 will decrease to 9.2% in the third quarter of 2023, and in the fourth quarter of 2023 it will be positioned within the target range, where it will remain until the end of the forecast horizon (second quarter of 2025). It was specified that the annual inflation will enter the target range in October this year.

It was cautioned that the current outlook is based on weaker external demand and continued moderation in inflationary pressures. International energy and food prices have stabilized in recent months, but in the medium to longer term supply shocks could contribute to a resumption of their upward trend.

The EB members also looked at aggregate demand, finding that aggregate demand over the entire forecast horizon will be below potential, driven by looser and declining real monetary conditions and the negative impact of external demand. At the same time, it was noted that the positive fiscal impulse will support domestic demand to some extent, with the exception of the last two quarters of the forecast.

At the same time, the trends anticipated in the previous rounds were found to remain valid. The inflation forecast was lowered insignificantly over the comparable period.

It has been emphasized that the risks and uncertainties of the forecast are high, but the balance of risks remains disinflationary. From the external environment, supply shocks caused by the war in Ukraine, the timing of monetary easing in the region and globally, energy and other raw material prices can be mentioned. The main domestic uncertainties include energy supply and prices, tariff adjustments, refugee flows, weather conditions and agricultural production this year and next year.

At the end of the monetary policy meeting, Mr. Radu Cuhai recommended for publication the scenario of the Inflation Report, August 2023 and the monetary policy measures, justifying that this decision is adopted in the context of the further propagation of the stimulatory effects conditioned by the NBM's decisions in the recent period, given the lags in their transmission and aims to anchor inflation expectations and ensure the monetary conditions necessary to bring and maintain inflation close to the inflation target of 5.0% in the medium-term.

Thus, following the analyses and findings of the meeting, the Executive Board decided by unanimous vote to maintain the base rate applied to the main short-term monetary policy operations at the current level of 6.00% annually. The interest rates on overnight loans and overnight deposits remained at their current levels of 8.00% and 4.00% annually respectively.

At the same time, the EB members decided to maintain the required reserve ratio of funds attracted in Moldovan lei and non-convertible currency at the current level of 34.0% of the calculation base, and the required reserve ratio of funds attracted in freely convertible currency – at the current level of 45.0% of the calculation base.

It was also noted that this decision is determined by the confirmation of the veracity of the last forecast of the National Bank of Moldova, as well as the new round of forecasts.

It was emphasized that the moderation of inflation and its forecast within the target range against the backdrop of excess liquidity and further decline in interest rates provide a favourable outlook for the economic activity.

In this regard, it was mentioned that the National Bank of Moldova adjusts in advance the conditions on the money, credit and foreign exchange markets, assuming the configuration of monetary policy as needed, thus aiming to maintain inflation close to the 5.0% target in the medium-term and creating all the necessary preconditions for the implementation of a macroeconomic policy mix associated with economic growth.

In these circumstances, the EB members cautioned that inflation is already not a determining factor that could influence the consumption and investment decisions of economic agents and households.

At the end of the meeting, it was emphasized that the NBM will continue to monitor the internal and external macroeconomic situation, the risks associated with the inflation development and, depending on them, will come up with new monetary policy measures necessary to maintain inflation close to the target in the medium-term.

**Decision adopted by the Executive Board of the NBM by unanimous vote:**

- 1. The base rate applied to the main short-term monetary policy operations is maintained at the current level of 6.00% annually.**
- 2. Interest rates are set:**
  - a) on overnight loans, at the level of 8.00% annually;**
  - b) on overnight deposits, at the level of 4.00% annually;**
- 3. The required reserve ratio from the funds attracted in MDL and non-convertible currency is maintained at the current level of 34.0% of the calculation base.**
- 4. The required reserve ratio from the funds attracted in freely convertible currency is maintained at the current level of 45.0% of the calculation base.**

**Voting results of the EB members**

FOR – 4

AGAINST – 0

**Chairman of the Executive Board****Secretary of the Executive Board****Octavian ARMASU****Sergiu SURDU**

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