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July 30, 2015. Press release of the National Bank of Moldova

Within the meeting of July 30, 2015, the Council of Administration of the NBM adopted the following decisions by unanimous vote:

1. to increase the base rate applied on main short-term monetary policy operations by 2.0 percentage points, from the level of 15.5 to 17.5 percent annually;

2. To increase the interest rates:
- **on overnight loans by 2.0 percentage points, from 18.5 to 20.5 percent annually;**
- **on overnight deposits by 2.0 percentage points, from 12.5 to 14.5 percent annually;**

3. To increase the required reserves ratio from financial means in MDL and non-convertible currency by 6.0 percentage points and set at the level of 32.0 percent of the base starting with the maintenance period of September 8, 2015 – October 7, 2015 of the required reserves in MDL;

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

The Council of Administration of the NBM approved the Inflation Report no.3, 2015, which will be presented at the press conference of August 6, 2015.

The annual inflation rate reached in June 2015 the level of 8.3 percent or by 0.2 percentage points more compared to the previous month, mainly due to higher contribution from core inflation and food prices by 3.8 and 3.2 percentage points, respectively.

In June 2015, the annual rate of core inflation[1] accounted for 11.1 percent, by 0.2 percentage points more compared to May 2015.

According to the information published by the NBS, exports and imports decreased by 18.3 and 25.0 percent in the first two months of the second quarter of 2015, compared to the same period of the previous year, while the industrial output increased by 1.8 percent.

Transport of goods decreased by 6.5 percent during January - June 2015, by 6.5 percent lower than the value recorded in the same period of the previous year.

In terms of consumer demand, the annual average real wage growth in the economy in April - May 2015 was 4.4 percent, by 2.2 percentage points lower than in the first quarter of 2015. Money transfers to individuals through the banks of the Republic of Moldova fell by 28.8 percent in January-June 2015 and by 28.9 percent in June 2015 compared with the same period of 2014.

At the end of June 2015, the balance of loans granted to economy decreased by 5.4 percent compared to the end of June 2014, while that of deposits increased by 4.9 percent.

In the second quarter of 2015, the average interest rates applied by banks to loans and deposits in national currency recorded an upward trend. Thus, the average annual interest rate on the loan portfolio in national currency increased by 0.83 percentage points compared to the first quarter of 2015, constituting 11.87 percent. The average interest rate on deposits in MDL has increased by 1.66 percentage points versus the previous quarter, registering a level of 9.82 percent.

The monetary policy continues to be affected by the complexity of risk balance, with a prevalence of inflationary risks. Weak economic activity in the euro area countries and the recession of the Russian Federation - the main trading partners of the Republic of Moldova maintain the risk of lowering of foreign currency income of households and domestic exporters in short-term, through foreign trade and remittances channel, which may subsequently influence the inflation. The escalation of geopolitical tension in the region could cause additional inflationary pressures.

The depreciation of the national currency since the beginning of this year has increased the inflationary pressures, which will subsequently determine in the future periods, through the prices of imported goods and tariffs of regulated services and later by second-round effects, the IPC to leave temporarily the upper limit of the range of ± 1.5 percentage point from the inflation target of 5.0 percent. It is anticipated that inflation will accelerate in the coming quarters, including due to the low calculation base of the previous year.

Against this background, within the meeting held on 30 July 2015, the members of the Council of Administration of the NBM decided by unanimous vote to increase the policy rate by 2.0 percentage points from 15.5 to 17.5 percent annually.

In order to sterilize excess liquidity accumulated in recent months and improve the transmission mechanism of monetary policy decisions, the Council of Administration took the decision to increase the required reserves ratio attracted in MDL and non-convertible currency by 6.0 percentage points up to 32.0 percent of the value of the base for the maintenance period of required reserves in MDL: 08 September 2015 - 07 October 2015. At the same time, the required reserves ratio from financial means attracted in freely convertible currency was maintained at the current level 14.0 percent of the base.

The decisions of the Council of Administration of 30 July 2015 are aimed at anchoring inflation expectations in the context of restoring and maintaining the inflation rate close to the target of 5.0 percent over the medium-term, with a possible deviation of ± 1.5 percentage points.

Over the next eight quarters, the output gap will be negative. The evolution of the national economy below its potential denotes a weak domestic demand, which would reduce future inflationary pressures.

According to a new round of forecasting, the average annual inflation rate for 2015 and 2016 is expected to record levels of 9.3 percent and 11.6 percent, respectively. NBM increased the average inflation forecast for 2015 and 2016 by 1.2 percentage points and 5.2 percentage points, respectively, compared to the previous forecast published in May 2015. Based on available data, due to the depreciation of the national currency and further increases in regulated tariffs, there is a risk that inflation may temporarily rise above the upper limit of the range of ± 1.5 percentage point from the target of 5.0 percent, with the return within the range of variation in the second quarter of 2017.

Inflation Report no.3, 2015 includes a more detailed assessment of the macroeconomic situation, inflation

forecast in the medium-term and potential risks and challenges that will be faced by the monetary policy in the next period. The report will be published on 06 August 2015 as scheduled.

In order to support the proper functioning of the interbank money market, the NBM will continue to manage firmly the liquidity excess through sterilization operations, according to the announced schedule.
National Bank will continue to offer banks liquidity, according to the schedule announced for 2015, through REPO operations with the term of 14 days, at a fixed rate equal to the base rate of the National Bank plus a margin of 0.25 points percentage.

NBM will further monitor and anticipate the domestic and international economic environment developments, including household consumption dynamics, remittances and changing foreign trade conditions, so that by the flexibility of operational framework specific for the inflation targeting strategy to ensure price stability in the medium term.

The next meeting of the Council of Administration of the NBM on monetary policy will take place on 26 August 2015, according to the announced schedule.

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

Evolution of the NBM interest rates [1]

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