

Inflation report 2013/4 (Monetary Policy Program Q4, 2014, Status report on implementation of the Monetary Policy Program, Q3, 2014)

2013-11-19

EXECUTIVE SUMMARY

The Central Bank forecasts suggest that in the course of the next 3 years the 12-month inflation would decline continuously and rest around the target while the economic growth would speed up in 2014 and stabilize around its long-term equilibrium. Yet in the 3rd quarter of 2013 the developments of the domestic economy marked slowing in economic growth rates and high inflationary environment. This was mainly determined by reduced private and public investment primarily due to contracted constriction volumes as well as the fiscal policy implemented since the beginning of the year, whilst direct and second-round effects of energy price increases contributed to high inflation (a total of 3.0 pp of contribution). Based on the 3rd quarter results, the 12-month inflation was 8.2% whereas the core inflation indicator was close to the upper bound of the confidence band, making up 5.3%.

Private consumption growth rates slowed down in the 3rd quarter amid high inflation and sluggish economic activity, under which conditions the private consumption growth for the period January-September is estimated 2.5% y/y. In the 3rd quarter private investment declined further than anticipated, with an estimated 9% y/y for the period January-September, which was primarily due to diminished value added in construction.

According to short-term forecasts, the private consumption in 2013 will grow by 2.7%, private investment growth rates will slow down to 7.0% and, based on the year's results, the fiscal policy will leave around 1.0 pp of contractionary impact. In 2013 the real growth of export of goods and services will be in the range of 7.0-9.0%; the real growth of import within 0.-1.0%.

In the outcome, the economic growth will reach 3.4-3.8% mainly attributable to the growths in agriculture and services (a total of roughly 3.8 pp of contribution). In view of the expansionary fiscal policy to be implemented in 2014, the economic growth rates are expected to accelerate especially in that period. In the forecast horizon the economic growth will stabilize within 4.6-6.0% and rest around its long-term equilibrium, reflecting

stabilization of private consumption growth rates and slow pace of recovering of private investment.

Thus, some recovery of private demand as well as expansionary effect of the fiscal policy in the forecast horizon will create a minor inflationary effect on domestic demand. In the external sector external demand remained sluggish in the 3rd quarter, chiefly due to economic developments in Russian economy. No significant inflationary patterns were observable in international markets of basic commodities and food products.

In the forecast horizon a slow pace of recovery in global economic growth rates is anticipated, under which conditions a steady low inflationary environment will be discernable in international markets of basic commodities and food products.

In the 3rd quarter, attributable to direct and indirect effects of increased energy prices, the 12-month inflation continued trending upward, making up 8.2% in end-September. To anchor inflation expectations and mitigate second-round effects of increased energy prices, the Central Bank tightened the monetary conditions in August by raising the refinancing rate by 0.5 pp to 8.5% (see details in section 3.1.1 Actual inflation and attainment of target).

However, further slowing of domestic demand as well as the Central Bank activity will provide for a lower inflation environment in the 4th quarter, under which circumstance inflation will reduce faster than anticipated. According to the Central Bank projections, in end 2013 inflation will decrease to 7.0% y/y which is still above the upper bound of the confidence band. Inflation, however, will keep on subsiding in the course of the first half of 2014 as well to return the target in the second half. In the 4th quarter of 2013 the Central Bank will loosen the monetary conditions to be consistent with the slowing of economic activity and mitigation of inflationary environment, whilst further directions of monetary policy to be carried out by the Central Bank will determine the pace of the fiscal policy, either.

Risks to deviation of inflation from the projected value are estimated as balanced in both short and medium-term perspectives. The primary risks are associated with the pace of recovery of global economy and the developments in the domestic economy. If such risks materialize, the Central Bank will react accordingly by maintaining the inflation target over the medium-term perspective.

[\(Monetary Policy Program Q4, 2014, Status report on implementation of the Monetary Policy Program, Q3, 2014\)](#)

