

# Serbia Watch: Slowdown in key rate hiking cycle, +25bp to 5.25%

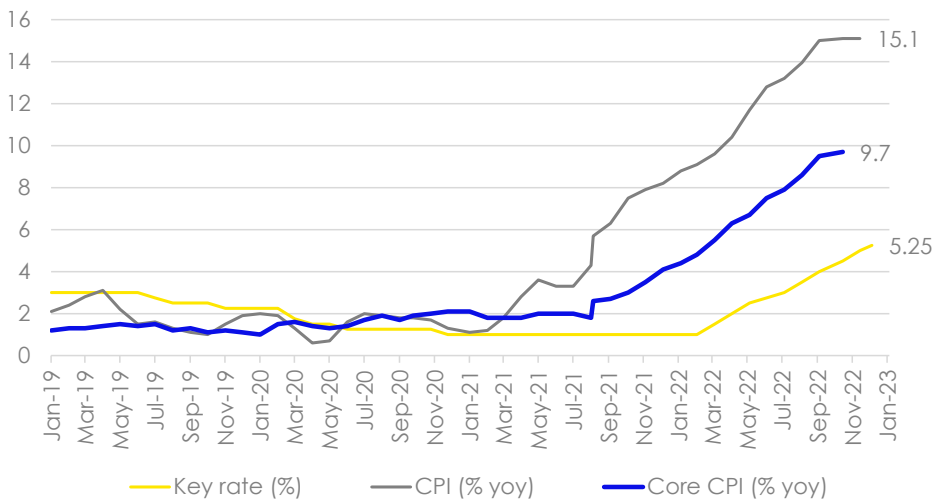
Following the inflation stabilization at the end of the year, Executive Board of the National Bank of Serbia (NBS) decided to slow down the pace of rate hiking cycle, increasing the benchmark rate by 25bp to 5.25%.

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The inflation trend losing pace, rate hikes also



Source: Statistical office, NBS, Raiffeisen Research

After the four 50bp hikes in the September-December/2022 period, the Executive Board of the National Bank of Serbia (NBS) decided to put the brakes on the hiking cycle. On the first key-rate-setting meeting this year, NBS raised the benchmark rate by 25bp to 5.25% supported by the mixture of factors: a) inflation stabilization in Serbia, b) inflation slowdown in the euro-zone, thus less inflationary impact from the imported prices and c) domestic economy slowdown in Q4/22. NBS is aware that the inflation slowdown in the euro-zone is driven by the energy prices decline on the global markets and gvt's measures to help citizens and companies deal with the energy crises. However, it is still uncertain whether this is really a sign of inflation peaking. This is because it is uncertain what the energy prices sentiment will be in the coming months.

Similar to the euro-zone inflation sentiment, domestic retail prices seem to be starting to lose steam, due to the energy prices fall. Thus, inflation grew by 0.5% mom in December 2022 after 1% mom growth in November 2022, supported by the decline in the transport prices (-3.2% mom), the slowdown in the clothes prices (+0.7% mom) after 1.3% mom growth in November 2022 due to seasonal sales and food and non-alcoholic beverages prices slowdown (+1.0% mom). Furniture, household equipment, and routine

**Ljiljana GRUBIC**

Analyst

+381 11 220-7178

ljiljana.grubic@raiffeisenbank.rs

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maintenance was the only item, having a larger increase (+2.6% mom) after 1.0% mom in November. The annualized figure was flat at 15.1% yoy like in November, supported by the food and non-alcoholic beverages prices (+23.4% yoy), housing, water, electricity, gas and other fuels (+19.3% yoy), apartment equipment and current maintenance (+18.2% yoy), transport (+9.2% yoy), and alcoholic beverages and tobacco (+7.8% yoy).

The benchmark rate was hiked by 425bp since April 2022 when the hiking started, and we expect it to continue, with the trajectory similar to the ECB i.e. less aggressive hiking (+25bp), but probably extending a bit. In that sense, we keep our key rate forecast at 6%, but now expecting the rate hiking to end in April, instead of the earlier assumption that it would be in March.

NBS expects that insofar monetary policy tightening in conjunction with the falling primary product prices on the global market (oil primarily) and easing bottlenecks in global supply chains will altogether support inflation slowdown in 2023. Still, thanks to the announced electric energy and gas price hikes in 2023, inflation is expected to remain elevated in H1, but to start mildly slowing in late spring due to the new agricultural season and more rapidly slowing in H2, while returning to the inflation target in 2024.

Exchange rate strengthening continued in early 2023, while FX reserves posted a new record high in December 2022 (EUR 19.4 bn), thanks to the disbursement of the EUR 985.6 mn under the recently approved IMF Stand-by arrangement and USD 1 bn disbursed under the Loan agreement with the Development Fund Abu Dhabi. IMF funds will be used for direct budget financing, Republic of Serbia FX obligations refinancing and other budget purposes. That said, the government has sufficient funds to support exchange rate stability, thus we will reconsider our EURRSD (eop) forecast for 2023 (118.3).

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Thomas Sternbach Legal and Compliance Raiffeisen Bank International AG Am Stadtpark 9, 1030 Wien Tel: +43-1-71707-1541 Fax: +43-1-71707-761541 thomas.sternbach@rbinternational.com


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## FABIAN BLASCH

📍 Austria  ,  
 ✉ [fabian.blasch@rbinternational.com](mailto:fabian.blasch@rbinternational.com)


## AMADEA HIESS

📍 Austria  ,  
 ✉ [amadea.hiess@rbinternational.com](mailto:amadea.hiess@rbinternational.com)


## MARKUS TSCHAPECK

📍 Austria  ,  
 ✉ [markus.tschapeck@rbinternational.com](mailto:markus.tschapeck@rbinternational.com)


## BRISIDA BUZI

📍 Albania  ,  
 ✉ [Brisida.BUZI@raiffeisen.al](mailto:Brisida.BUZI@raiffeisen.al)

## ARISTEA VLLAHU

📍 Albania  ,  
 ✉ [Aristea.Vllahu@raiffeisen.al](mailto:Aristea.Vllahu@raiffeisen.al)


## IVONA ZAMETICA

📍 Bosnia Herzegovina  ,  
 ✉ [ivona.zametica@raiffeisengroup.ba](mailto:ivona.zametica@raiffeisengroup.ba)


## ELIZABETA SABOLEK-RESANOVIC

📍 Croatia  ,  
 ✉ [elizabeta.sabolek-resanovic@rba.hr](mailto:elizabeta.sabolek-resanovic@rba.hr)

## DAVID VAGENKNECHT

📍 Czech Republic  ,  
 ✉ [david.vagenknecht@rb.cz](mailto:david.vagenknecht@rb.cz)


## ZOLTÁN TÖRÖK

📍 Hungary  ,  
 ✉ [torok.zoltan@raiffeisen.hu](mailto:torok.zoltan@raiffeisen.hu)


## ANDREEA-ELENA DRAGHIA

📍 Romania  ,  
 ✉ [Andreea-Elena.DRAGHIA@raiffeisen.ro](mailto:Andreea-Elena.DRAGHIA@raiffeisen.ro)


## GREGORY CHEPKOV

📍 Russia  ,  
 ✉ [grigory.chepkov@raiffeisen.ru](mailto:grigory.chepkov@raiffeisen.ru)

## TIBOR LORINCZ

📍 Slovakia  ,  
 ✉ [tibor\\_lorincz@tatrabanka.sk](mailto:tibor_lorincz@tatrabanka.sk)

## GUNTER DEUBER

📍 Austria  ,  
 ✉ [gunter.deuber@rbinternational.com](mailto:gunter.deuber@rbinternational.com)


## MATTHIAS REITH

📍 Austria  ,  
 ✉ [matthias.reith@rbinternational.com](mailto:matthias.reith@rbinternational.com)

## ANNE VALDER

📍 Austria  German,  
 ✉ [anne.valder@rbinternational.com](mailto:anne.valder@rbinternational.com)


## VALBONA GJEKA

📍 Albania  ,  
 ✉ [valbona.gjeka@raiffeisen.al](mailto:valbona.gjeka@raiffeisen.al)


## OLGA ZHEGULO

📍 Belarus  ,  
 ✉ [olga.zhegulo@priorbank.by](mailto:olga.zhegulo@priorbank.by)

## MIRZA ZORNIC

📍 Bosnia Herzegovina  ,  
 ✉ [mirza.zornic@raiffeisengroup.ba](mailto:mirza.zornic@raiffeisengroup.ba)


## ZRINKA ZIVKOVIC-MATIJEVIC

📍 Croatia  ,  
 ✉ [zrinka.zivkovic-matijevic@rba.hr](mailto:zrinka.zivkovic-matijevic@rba.hr)

## LEVENTE BLAHÓ

📍 Hungary  ,  
 ✉ [levente.blaho@raiffeisen.hu](mailto:levente.blaho@raiffeisen.hu)


## DOROTA STRAUCH

📍 Poland  ,  
 ✉ [dorota.strauch@raiffeisen.pl](mailto:dorota.strauch@raiffeisen.pl)


## IONUT DUMITRU

📍 Romania  ,  
 ✉ [Ionut.Dumitru@raiffeisen.ro](mailto:Ionut.Dumitru@raiffeisen.ro)


## STANISLAV MURASHOV

📍 Russia  ,  
 ✉ [stanislav.murashov@raiffeisen.ru](mailto:stanislav.murashov@raiffeisen.ru)

## SERHII KOLODII

📍 Ukraine  ,  
 ✉ [serhii.kolodii@raiffeisen.ua](mailto:serhii.kolodii@raiffeisen.ua)


## CASPER ENGELEN

📍 Austria  ,  
 ✉ [casper.engelen@rbinternational.com](mailto:casper.engelen@rbinternational.com)


## GOTTFRIED STEINDL

📍 Austria  ,  
 ✉ [gottfried.steindl@rbinternational.com](mailto:gottfried.steindl@rbinternational.com)


## FRANZ ZOBL

📍 Austria  ,  
 ✉ [franz.zobl@rbinternational.com](mailto:franz.zobl@rbinternational.com)


## FJORENT RRUSHI

📍 Albania  ,  
 ✉ [Fjorent.Rrushi@raiffeisen.al](mailto:Fjorent.Rrushi@raiffeisen.al)


## ASJA GRDJO

📍 Bosnia Herzegovina  ,  
 ✉ [asja.grdjo@raiffeisengroup.ba](mailto:asja.grdjo@raiffeisengroup.ba)


## ANA LESAR

📍 Croatia  ,  
 ✉ [ana.lesar@rba.hr](mailto:ana.lesar@rba.hr)

## HELENA HORSKA

📍 Czech Republic  ,  
 ✉ [Helena.Horska@rb.cz](mailto:Helena.Horska@rb.cz)


## GERGELY PÁLFFY

📍 Hungary  ,  
 ✉ [gergely.palffy@raiffeisen.hu](mailto:gergely.palffy@raiffeisen.hu)

## NICOLAE COVRIG

📍 Romania  ,  
 ✉ [Nicolae.Covrig@raiffeisen.ro](mailto:Nicolae.Covrig@raiffeisen.ro)

## ANASTASIA BAYKOVA

📍 Russia  ,  
 ✉ [ABAIKOVA@raiffeisen.ru](mailto:ABAIKOVA@raiffeisen.ru)

## LJILJANA GRUBIC

📍 Serbia  ,  
 ✉ [ljiljana.grubic@raiffeisenbank.rs](mailto:ljiljana.grubic@raiffeisenbank.rs)

## OLEKSANDR PECHERYTSYN

📍 Ukraine  ,  
 ✉ [oleksandr.pecherytsyn@raiffeisen.ua](mailto:oleksandr.pecherytsyn@raiffeisen.ua)

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