

Serbia Watch: Key rate hiked again, +50bp to 4.5%

Despite weak GDP data for Q3 (+1.1% yoy), and amid high inflation (Sept: 14%) the Executive Board of the National Bank of Serbia (NBS) decided to hike the benchmark rate by 50bp third time in a row, to 4.5%.

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The NBS accelerated the hiking dynamics in September, rising the key rate by 50bp at each meeting until the November. Thus, the accumulated key rate growth since when the rate hiking started (April), now stands at 350 bp. According to the NBS, rising costs and inflation (mostly import prices) have supported today's decision, though NBS is increasingly focusing on inflation expectations stabilization as well. Accelerated key rate hiking dynamics by the Fed and ECB and growing inflationary pressure on the global markets are also fueling the local benchmark rate growth. Nonetheless, 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. According to the November mid-term inflation projection, NBS now expects headline inflation to stay elevated until the end of the year and in early 2023, but will start slowing down afterwards, especially in H2 2023 and will return to the inflation target (3% +/- 1.5pp) in 2024. Inflation in September came at 14.0% supported by the drought-driven food inflation, while core inflation accelerated as well to 8.6% yoy due to import price growth.

Concerning the economic sentiment, NBS expects that after the GDP slowdown in Q3 (+1.1% yoy flesh estimate), the economy will be weaker in the remainder of the year and at the beginning of 2023, but will accelerate after, supported by external demand recovery and investment projects (infrastructure).

Exchange rate strengthening continued in late autumn supported by the FX flows and less FX demand by energy importers amid good weather conditions. We do not expect many surprises towards the end of the year and EURRSD could even hover around the current level (117.2-117.35), which makes our 117.6 projection (eop) for 2022 ready for revision.

Given that now NBS expects inflation will remain high in the next quarter or two, and that the economic deceleration will be only of temporary nature, reviving again around spring, we could expect bold rate hiking down the road, even above our current forecast (Q1/2023: 5%). Thus we will reconsider our key rate forecast for this year (4.75% eop) and next year (5.0%) in order to assess whether there is potential for more rate hikes.

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