



NATIONAL BANK OF SERBIA

**REPORT ON THE RESULTS
OF THE INFLATION EXPECTATION SURVEY**

June 2016

Belgrade, July 2016

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Introductory note

Indicators of inflation expectations of economic agents are an important factor in the process of monetary policy decision-making in an inflation targeting regime. The effectiveness of the inflation targeting strategy is measured by the degree of stability of inflation expectations and by how firmly they are anchored within the target tolerance band. Stable and well-anchored inflation expectations contribute to greater credibility of the monetary policy framework. Consistent with best international practice, after introducing the inflation targeting regime in January 2009, the NBS began monitoring and analysing inflation expectations of economic agents, drawing on the inflation expectations survey, conducted for the NBS by Ninamedia since December 2014. Survey participants are classified into four sectors (the financial sector, corporate sector, trade unions and households) and asked to state their one-year ahead price growth expectations, and since March 2014, also their medium-term, i.e. two-year ahead, expectations for y-o-y price growth.

Summary

According to the June survey results, the financial and corporate sectors believe that price stability will be maintained both one and two years ahead. One-year ahead inflation expectations stayed unchanged across all sectors, save for the household sector where expectations declined from May. Medium-term expectations of the financial sector and trade unions decreased, while those of the corporate and household sectors stayed at the May level.

According to the results of the Ninamedia survey, one-year ahead inflation expectations of the *financial sector* stayed at 2.5% for the fourth consecutive month. They have been moving within the target tolerance band for over two and a half years now.

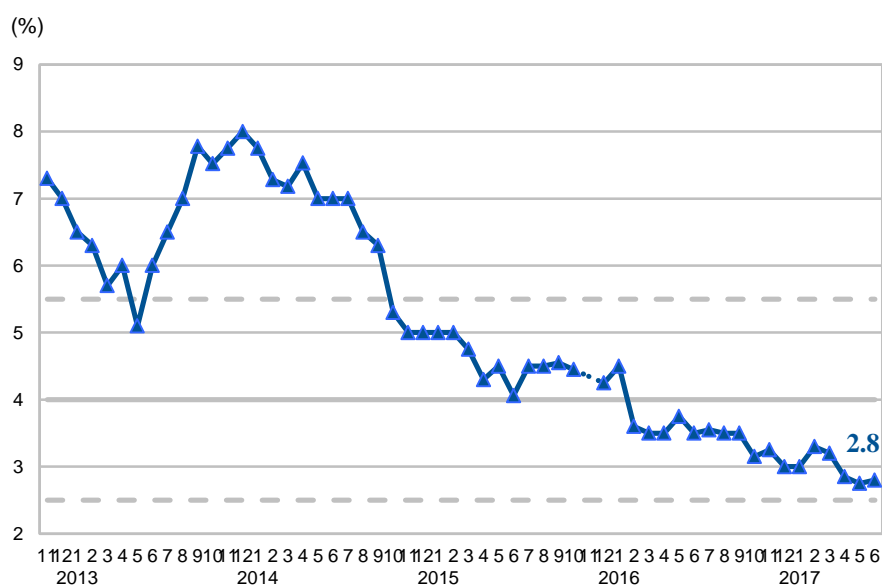
One-year ahead inflation expectations of *corporates* stayed at 2.0% for the third consecutive month. In June, one-year ahead *household* inflation expectations came at 5.0%, while those of *trade unions* equalled 2.5%.

Medium-term inflation expectations of all sectors stayed within the target tolerance band, except in the case of corporates, which lowered their expectations.

Inflation expectations of the financial sector

According to the Ninamedia survey, one-year ahead inflation expectations of the financial sector have been within the target tolerance band for over two and a half years now (since October 2013). In June, they came at 2.5%, staying at the lower bound of the target tolerance band for the fourth consecutive month. Bloomberg survey results also show that financial sector expectations have been within the target tolerance band since October 2013. In July, they inched down to 2.85% (from 3.0% in June).

Chart 1 Composite measure of inflation expectations of the financial sector



Sources: NBS, Ipsos, Ninamedia and Bloomberg.

The composite measure of one-year ahead inflation expectations of the financial sector¹ (covering the results of Ninamedia and Bloomberg surveys) rose mildly, coming at 2.8% in June.

Two-year ahead inflation expectations of the financial sector have been within the target tolerance band since the inception of the survey (March 2014) and measured 2.8% in June.

¹ Calculated by weighting individual responses by the size of the respondent's share in total assets of the surveyed financial institutions. Institutions participating in both surveys are assigned the arithmetic mean of the responses provided in Ninamedia and Bloomberg surveys. Hence, banks with a larger market share have a greater influence on the aggregate result, which corresponds to the real situation, as their impact on economic flows is somewhat stronger.

Inflation expectations of the corporate sector

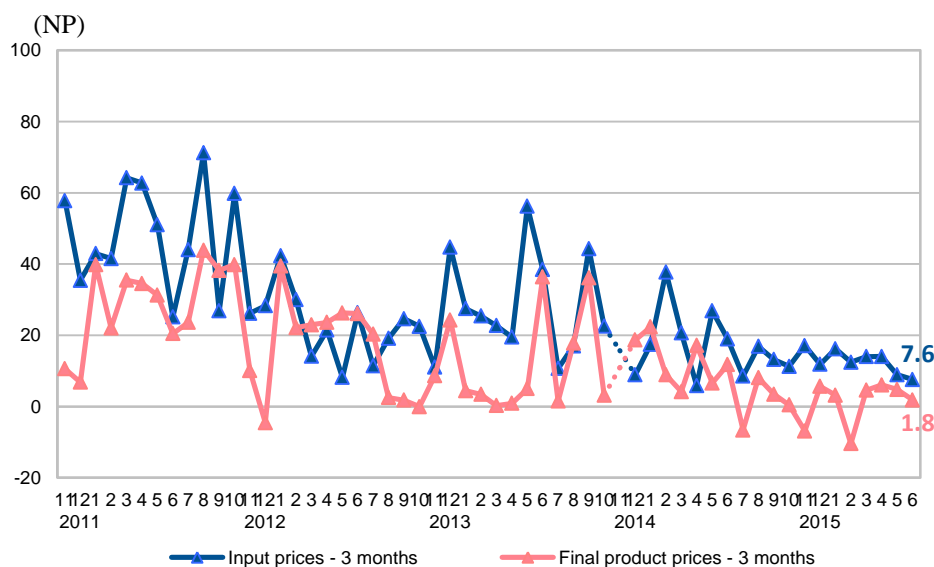
One-year ahead inflation expectations of the corporate sector have been at 2.0% for the third consecutive month. Low and stable inflation expectations of the corporate sector reflect weaker cost pressures thanks to low prices of oil and other primary commodities, and low inflation at home and abroad.

The net percentage² (NP) of enterprises expecting an increase in prices of *inputs* over the next three months came at 7.6 pp in June (vs. 8.9 pp in May). The NP of respondents expecting an increase in prices of *final products* in the same period was 1.8 pp (vs. the May NP figure of 4.8 pp). **The majority of respondents anticipated that prices of both inputs (91.1%) and final products (97.2%) would stagnate in the next three months.** In terms of expectations for the next twelve months, the results in June are as follows: the NP of enterprises expecting an increase in prices of *inputs* is 19.9 pp (vs. 16.5 pp in May), and of those anticipating an increase in prices of *final products* 25.7 pp (vs. 22.6 pp in May).

As regards production/trade, the NP of respondents expecting an increase in the next three months rose to 44.3 pp (from 39.9 pp in May), **while the NP of respondents anticipating an increase in production/trade in the next twelve months was 49.0 pp (vs. 38.5 pp in May).**

² Calculated as the difference between the share of enterprises expecting prices to increase and enterprises expecting prices to decrease, weighted by operating income.

Chart 2 Expectations of the corporate sector regarding movements in input and final product prices in the next three months



*Above zero indicates growth, and below zero decline.
Source: Ipsos/Ninamedia.

Inflation expectations of trade unions

For the third consecutive month, trade unions expect y-o-y inflation (June 2017) to equal 2.5%. Their medium-term expectations dropped from 3.25% in May to 2.75% in June, and have been moving within the target tolerance band since March 2015.

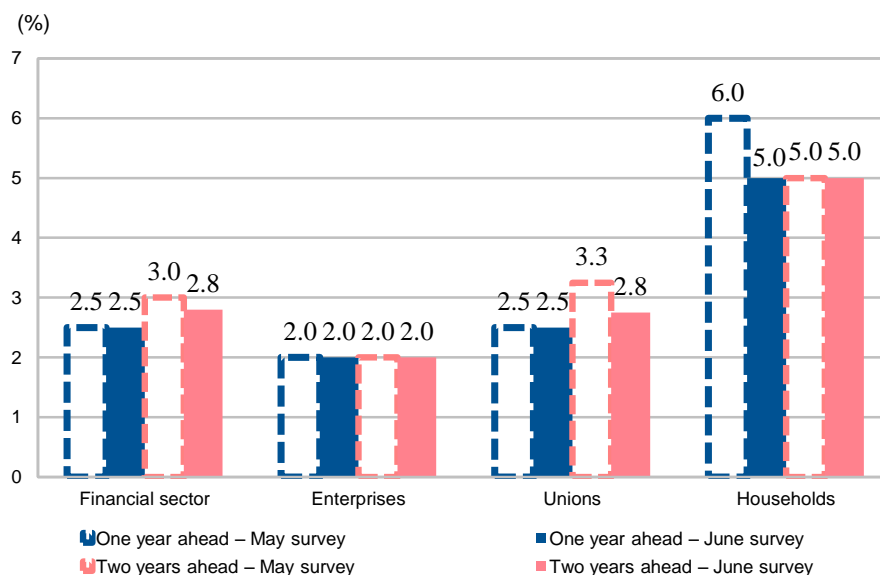
Inflation expectations of households

Quantitative inflation expectations of households

Inflation expectations of households stood firmly at 5.0% from October to March when they started exhibiting more volatility, moving closer to the upper bound of the target tolerance band. In June, they re-entered the band and came at 5.0% (vs 6.0% in May).

Staying at 5.0%, the two-year ahead inflation expectations of households remained unchanged for the seventeenth consecutive month, which indicates that households expect that inflation will stabilise within the target tolerance band over the medium run.

Chart 3 Expected y-o-y inflation one and two years ahead

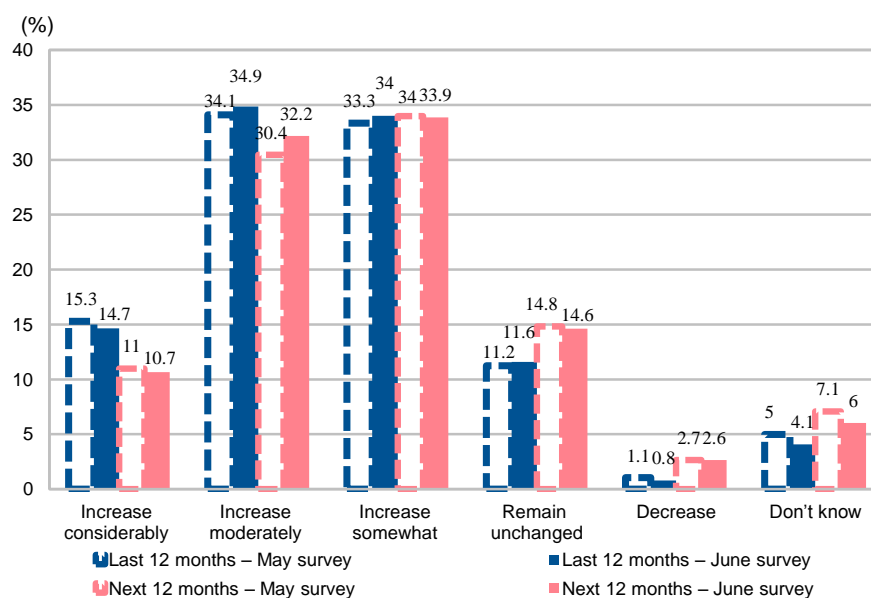


Source: Ninamedia.

Qualitative inflation expectations of households

Descriptive (qualitative) expectations of households regarding a rise in prices indicate that the majority of respondents (66.1%) expect a moderate or mild increase in prices in the next twelve months, 14.6% of respondents expect no change in prices, and 2.6% anticipate a fall, while 6.0% of respondents said they did not know. The share of respondents anticipating prices to increase considerably in the coming twelve months touched a new low of 10.7% (vs. 11.0% in May).

In the prior period, the number of respondents anticipating a considerable increase in prices trended down in favour of respondents anticipating prices to rise moderately, increase somewhat or remain unchanged. Such trends confirm the creation of a predictable and stable economic environment, and facilitate the achievement of the main goal of the monetary policy in the medium run.

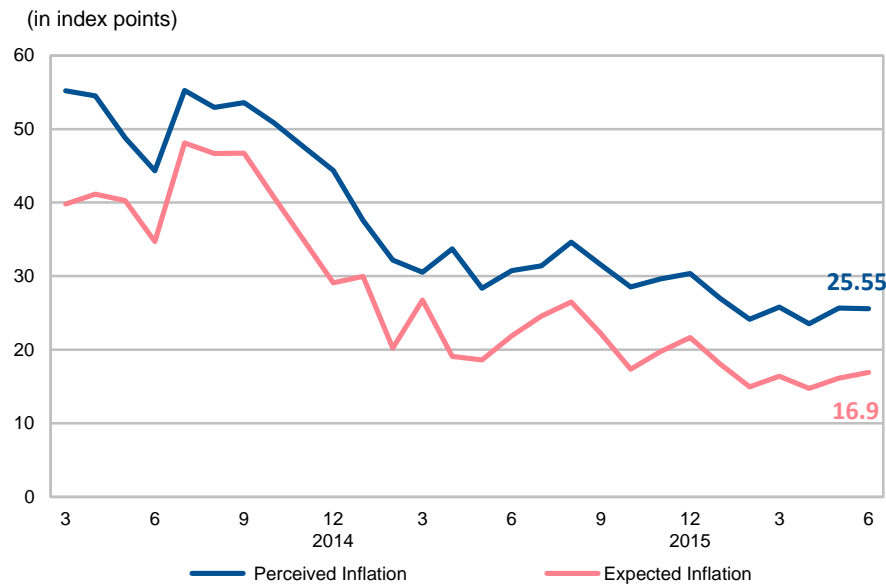
Chart 4 Distribution of household responses by perceived (recorded) and expected inflation

Source: Ninamedia.

The fact that the perceived (current) inflation index was above the expected inflation index³ **signals that one part of the population, who feel that prices increased in the past twelve months, do not expect the trend to continue over the next 12 months.** Both indicators have been on a downward path since mid-2014.

³ The indicator represents the difference between the weighted share of respondents who assess that prices increased more than somewhat and those assessing that prices remained unchanged or decreased. For details, see Text box 2 of the Inflation Report – February 2016.

Chart 5 Perceived and expected inflation of households



Source: Ninamedia.