



NATIONAL BANK OF SERBIA

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

July 2016

Belgrade, August 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 July survey results, the financial and corporate sectors expect that price stability will be maintained both one and two years ahead. One-year ahead inflation expectations of the financial sector and trade unions declined, while staying unchanged across the corporate and household sectors, compared to the previous survey. Medium-term expectations of all observed sectors stayed at the June level, except for those of the financial sector, which declined.

According to the results of the Ninamedia survey, one-year ahead inflation expectations of the *financial sector* dropped to 2.0% in July.

One-year ahead inflation expectations of *corporates* stayed at 2.0% for the fourth consecutive month. In July, one-year ahead *household* inflation expectations came at 5.0%, while those of *trade unions* equalled 2.25%.

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

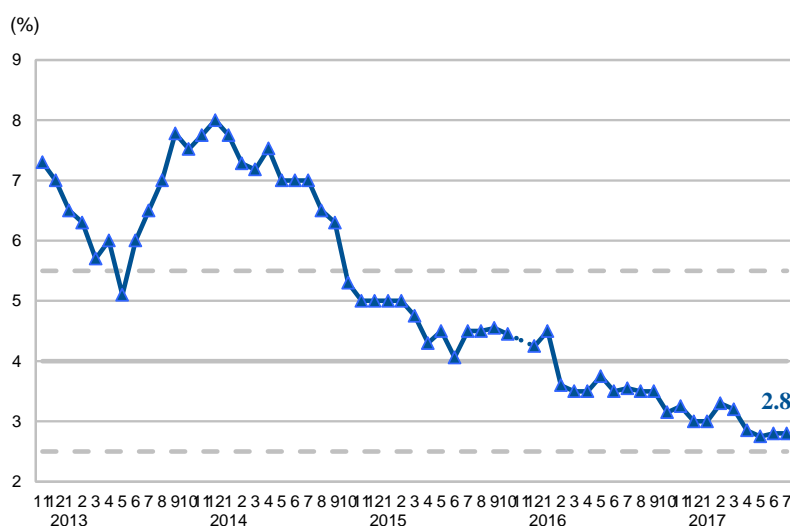
Firmly anchored inflation expectations are one of the prerequisites for achieving low, stable and predictable inflation. The fact that inflation expectations in Serbia are well anchored confirms the credibility of the NBS measures and indicates the absence of major inflationary and disinflationary pressures.

Inflation expectations of the financial sector

According to the Ninamedia survey, one-year ahead inflation expectations of the financial sector declined to 2.0% in July, dropping from a month before when they stood at the lower bound of the target tolerance band of 2.5%.

Bloomberg survey results show that financial sector expectations have been within the target tolerance band since October 2013. In August, they came at 2.8%, nearly unchanged from the July level of 2.85%.

Chart 1 Composite measure of inflation expectations of the financial sector



Sources: NBS, Ipsos, Ninamedia and Bloomberg.

In July, the composite measure of one-year ahead inflation expectations of the financial sector¹ (covering the results of Ninamedia and Bloomberg surveys) stayed at 2.8%.

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 2.5% in July.

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

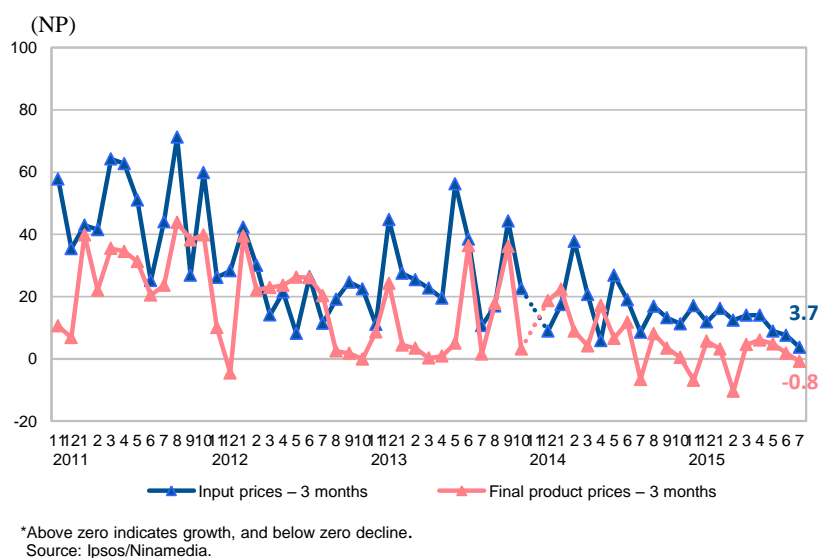
One-year ahead inflation expectations of the corporate sector stayed firmly at 2.0% for the fourth consecutive month. Low and stable inflation expectations of the corporate sector reflect weaker cost pressures thanks to lower prices of oil and other primary commodities, and low inflation at home and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

The net percentage² (NP) of enterprises expecting an increase in prices of *inputs* over the next three months came at 3.7 pp in July (vs. 7.6 pp in June). The NP of respondents expecting a drop in prices of *final products* in the same period was 0.8 pp (vs. the June NP figure of 1.8 pp of respondents who expected an increase). **The majority of respondents anticipated that prices of both inputs (95.8%) and final products (96.9%) would stagnate in the next three months.** In terms of expectations for the next twelve months, the results in July are as follows: the NP of enterprises expecting an increase in prices of *inputs* is 19.7 pp (vs. 19.9 pp in June), and of those anticipating an increase in prices of *final products* 19.4 pp (vs. 25.7 pp in June).

As regards production/trade, the NP of respondents expecting an increase in the next three months dropped to 30.3 pp (from 44.3 pp in June), as did the NP of respondents anticipating an increase in production/trade in the next twelve months, which came at 38.5 pp (from 49.0 pp in June).

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



Inflation expectations of trade unions

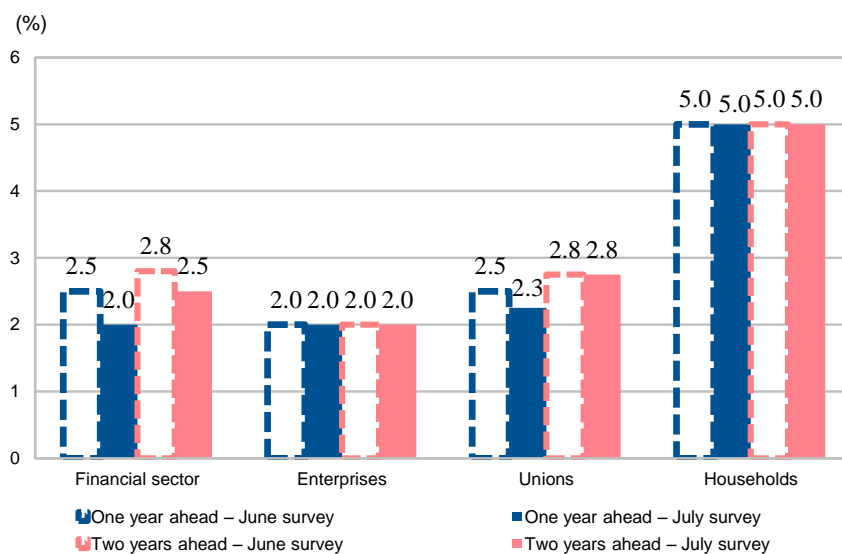
One-year ahead (i.e. July 2017) expectations of trade unions came at 2.25%, sliding from the lower bound of the target tolerance band of 2.5% where they had previously stood for three consecutive months. Medium-term expectations of trade unions stayed at the June level of 2.75%, and have been moving within the target tolerance band since March 2015.

Inflation expectations of households

Quantitative inflation expectations of households

Inflation expectations of households have stood firmly at 5.0% from October 2015 to July 2016 (rising shortly to 6.0% in March and May).

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

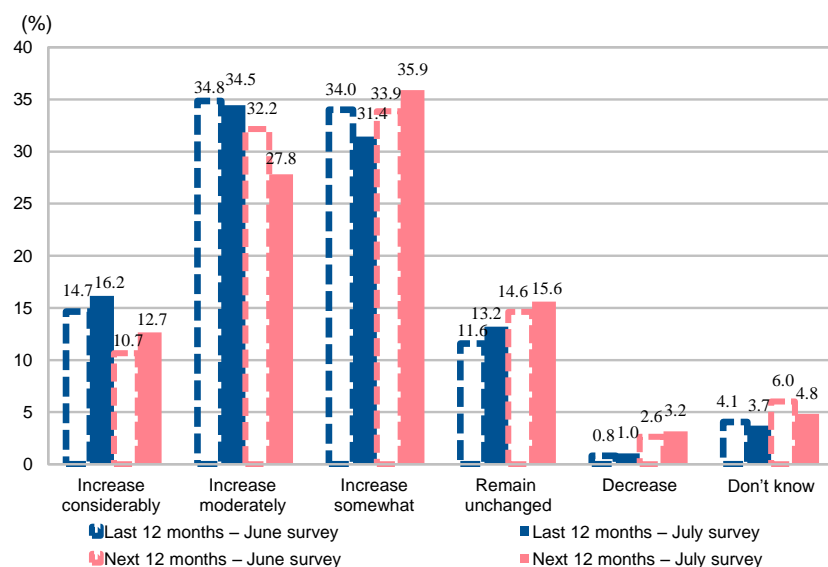
Chart 3 Expected y-o-y inflation one and two years ahead

Source: Ninamedia.

Qualitative inflation expectations of households

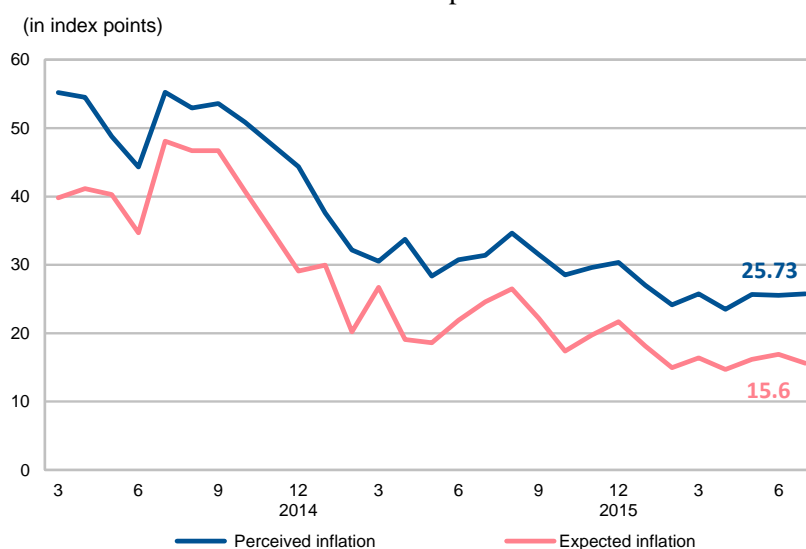
Descriptive (qualitative) expectations of households regarding a rise in prices indicate that the majority of respondents (63.7%) expect a moderate or mild increase in prices in the next twelve months, 15.6% of respondents expect no change in prices, and 3.2% anticipate a fall, while 4.8% of respondents said they did not know. The share of respondents anticipating prices to increase considerably in the coming twelve months recovered from the June low of 10.7%, coming at 12.7% in July.

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 a predictable and stable economic environment which facilitates 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.

Chart 5 Perceived and expected inflation of households

Source: Ninamedia.

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.