Research

INFLATION AND MONETARY POLICY IN BLACK SEA COUNTRIES

BLACK SEA BULLETIN
ISSUE 9

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Tbilisi, 2023

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INTRODUCTION

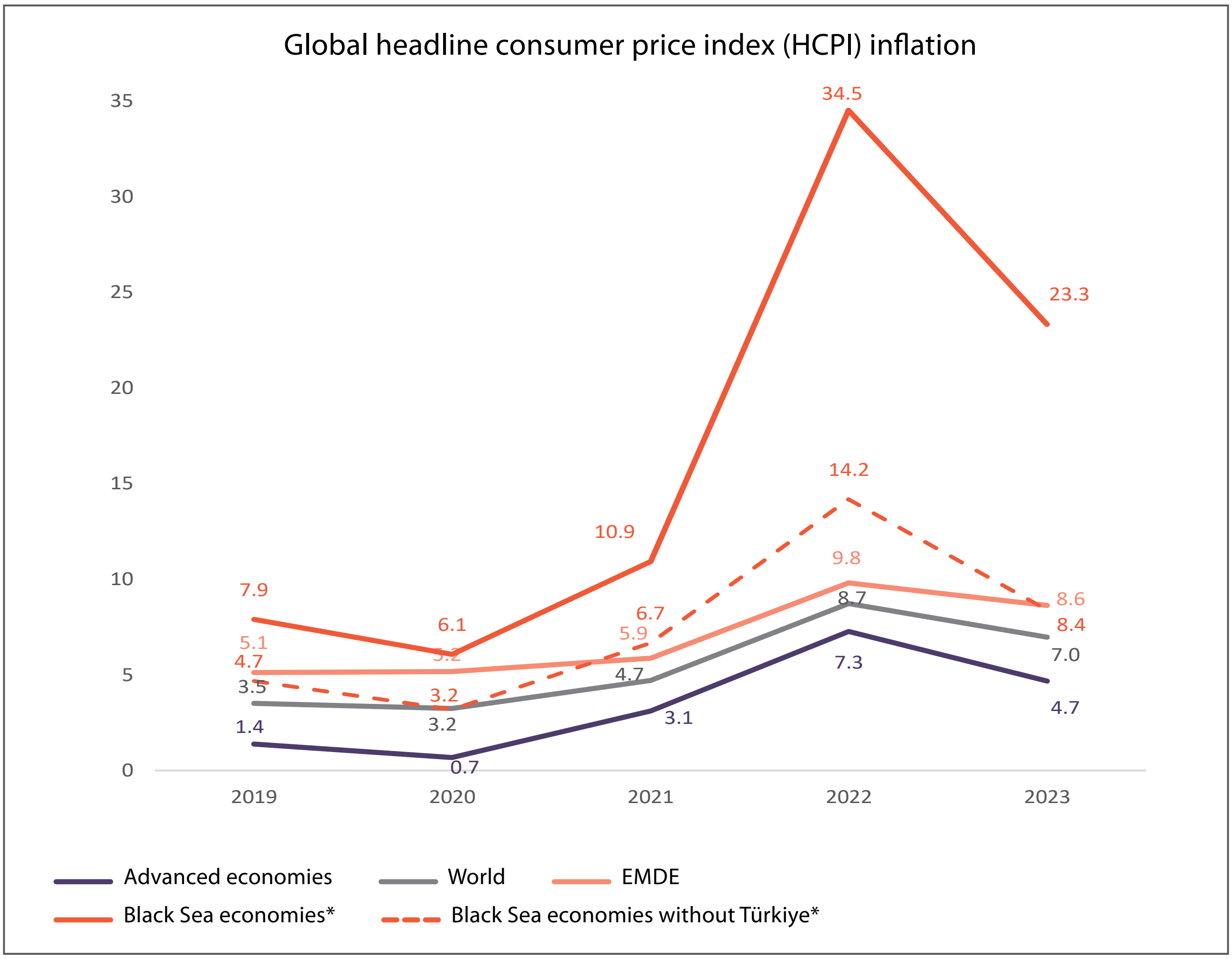
The Black Sea region has often been referred to as a gateway between Europe and Asia. However, the potential of the region has not been fully realized due to a lack of political and economic cooperation among the countries therein. Notably, irrespective of their geographical proximity, there are some significant political and economic differences among them. Moreover, since the outbreak of Russia's war on Ukraine, it has become essential to find alternative trade routes that bypass Russia to transport goods from the East to the West. In this regard, the Black Sea region has come under the spotlight with the Black Sea corridor highlighted as a potential option. In this context, it became even more important to analyze economic indicators and policy approaches implemented in Black Sea countries, which is the aim of this bulletin. In particular, the bulletin aims to understand and assess how those states are performing in different areas, to detect what similarities and differences can be found between the countries of the region, as well as to compare the performance of Black Sea countries with that of the rest of the world.

Since mid-2020, when stringent restrictions were imposed to combat the spread of the COVID-19 pandemic, inflation has been running at multi-decade highs in many countries across the globe. In 2022 in particular, inflationary pressures from pandemic-related disruptions were exacerbated by the Russo-Ukrainian War and spiking food and energy prices. In response, central banks implemented different monetary policy approaches in an attempt to stabilize the situation. Against this background, recent inflationary trends and monetary policy approaches adopted by economically diverse Black Sea countries are analyzed and compared in this issue of Black Sea bulletin.

The bulletin starts with a discussion of global inflation trends, before proceeding to overview of headline and core CPI in each Black Sea country from January 2020 till May 2023. It then advances to examine the monetary policy approaches adopted by the Black Sea countries. To conclude, the final chapter summarizes the inflation and monetary policy trends of Black Sea countries and provides some recommendations.

GLOBAL INFLATION TRENDS

Graph 1



Source: International Monetary Fund (IMF), World Economic Outlook Database, April 2023
** Calculations of PMC RC*

Global headline inflation fell in 2020 as downward price pressures stemming from the decline in aggregate demand caused by the COVID-19 pandemic and lower fuel prices turned stronger than upward pressure from supply disruptions.[1] However, since mid-2020, global inflation has risen sharply with a combination of rebounding global demand, sustained supply chain disruptions, and soaring food and energy prices.[2] As a result of these pressures, global headline inflation remained high throughout 2021, increasing from 2.9% in 2020 to 6.3%. Such upward inflationary pressures were exacerbated by Russia's invasion of Ukraine in February 2022. As a result of these pressures, global headline inflation remained high throughout 2021, increasing from 3.2% in 2020 to 4.7%. Such upward inflationary pressures were exacerbated by Russia's invasion of Ukraine in February 2022. As a result, global headline inflation reached 8.7% in 2022, which was approximately triple the corresponding rate in 2020. In emerging market and developing economies (EMDE) headline inflation in 2022 was 1.1 pp higher than the global average (9.8%) and in advanced economies inflation was 1.4 pp lower (7.3%).

1 IMF, June 2020. World Economic Outlook Update. A Crisis Like No Other, An Uncertain Recovery.

2 World Bank, June 2022. Global Economic Prospects.

Although global headline inflation started to decline in 2023 (according to the baseline scenario, global headline inflation is forecast to fall to 7.0% in 2023) as central banks have raised interest rates and food and energy prices have decreased[3], underlying price pressures have proved to be much stickier than anticipated even a few months ago (in April, the IMF's inflation projections underwent a sizable upward revision of 0.4 pp in relation to their January update).[4] IMF predicts that the massive and synchronous tightening of monetary policy by most central banks would simultaneously result in inflation moving back toward its targets. Though recently, negative side effects of the fast rise in policy rates have also became apparent.[5] The generally strong liquidity and capital positions of banks suggested that they would be able to adapt smoothly to the impacts of monetary policy tightening. Nevertheless, tighter monetary policy conditions have exposed some outliers, namely banks with poor internal interest rate risk management practices which have heavily relied on the continuation of the extremely low nominal interest rates of recent years.[6] The US's regional banks – Silicon Valley Bank, Signature Bank, and First Republic – were among those outliers to have come under acute stress as a result of a steep rise in interest rates. Meanwhile, uninsured depositors ran from such banks out of fear that the banks' losses would materialize and would have to sell securities to meet deposit outflows. The collapse of confidence in Credit Suisse – a globally significant bank – has further roiled financial markets. Even though both US and Swiss authorities took strong and rapid action to protect all depositors and have been able to contain the spread of the crisis so far, trust in the financial system has been compromised. Indeed, some depositors and investors have become highly sensitive to any news, as they struggle to distinguish between a breadth of vulnerabilities across financial institutions and predict their implications for the economy.

PMC RC has also calculated average inflation for the Black Sea region, using the IMF data (the data was weighted by GDP valued at purchasing-power-parity). The inflation trends in the Black Sea region were in line with global inflation trends – with decrease in 2020 (by 1.8 pp from 7.9 in 2019 to 6.1) and sharp spike in 2022 (from 10.9 in 2021 to 34.5 in 2022). And like global inflation, average inflation of Black Sea countries in 2023 while still remaining on high level (23.3%) is predicted to considerably decrease compared to 2021 (by 11.2 pp). The data also suggests that inflation in the Black Sea region was higher than global inflation, as well as higher than inflation in advanced economies and emerging markets and developed economies (EMDE), throughout the whole analyzed period (2019-2023). The gap between the Black Sea and those regions especially widened in 2022, when average inflation of Black Sea countries reached 34.5%, which was about 4 times the global average. Though such a high inflation in the region is mainly attributed to Türkiye, which not only has extraordinarily high inflation, but also has more weight due to its high GDP. Accordingly, inflation for Black Sea countries excluding Türkiye is much lower. In 2019-2020 average inflation in Black Sea countries excluding Türkiye was lower than inflation of EMDE region (in 2020 average inflation in Black sea amounting 3.2% was equal to global average). In 2021-2022 even excluding Türkiye inflation of Black Sea region was higher than global inflation and inflation in EMDE (and obviously much higher than in advanced economies). Though in 2023, average inflation in Black Sea region excluding Türkiye is predicted to decrease to 8.4% which is slightly below the average inflation for EMDE (8.6%).

3 https://www.worldbank.org/en/news/press-release/2023/04/27/commodity-prices-to-register-sharpest-drop-since-the-pandemic

4 IMF, April 2023. World Economic Outlook. A Rocky Recovery.

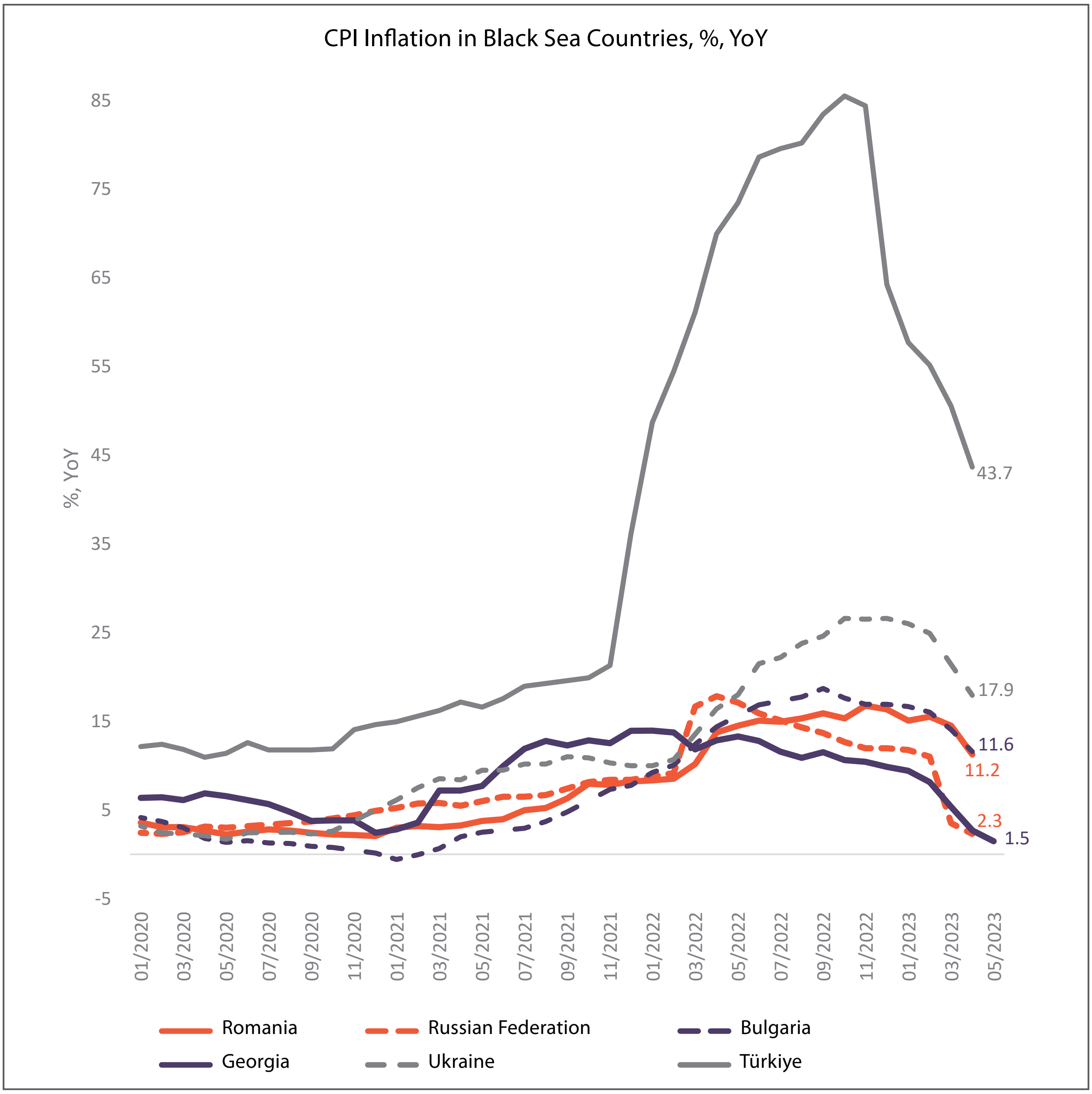
5 https://www.imf.org/en/Blogs/Articles/2023/04/11/global-financial-system-tested-by-higher-inflation-and-interest-rates

6 IMF, April 2023. Global Financial Stability Report.

INFLATION IN BLACK SEA COUNTRIES

Inflation has recently been hitting a multidecade high in many countries, and the Black Sea region has been no exception. In particular, high inflation trends are especially pronounced in this region, as it consists of the two countries directly involved in the war – Ukraine and Russia - as well as neighboring countries that have close economic ties with one or both of the protagonists. Of note, Türkiye with its record high inflation has come under not only regional, but even the global spotlight.

Graph 2



Source: National banks of Black Sea countries, May 2023

Looking at CPI inflation trends in Black Sea countries from January 2020 until May 2023, **Türkiye** emerges as an outlier in the region. The level of inflation in Türkiye has been higher compared to other countries in the region throughout the whole analyzed period. The difference in this regard has been especially noticeable since November 2021, when Türkiye's inflation started to rise steeply, before peaking at 85.5% in October 2022. The currency crisis (i.e. the strong depreciation of the Turkish Lira), as well as the Turkish government's expansionary fiscal policy (including tax cuts and increased government spending) have contributed to high inflation in Türkiye. Critically, its central bank has maintained a loose monetary policy (low interest rates and increased money supply). However, despite traditionally accepted economic theories suggesting the opposite – in order to control high inflation, the central bank should instead raise interest rates and decrease money supply.[7] From January 2023 onward, inflation in Türkiye, though still abnormally high, has started to fall, but this can be largely attributed to the base effect, as well as the stabilization of prices for energy imports.[8] The reduced inflation rate comes in the wake of staggeringly destructive earthquakes in Türkiye, though the Turkish Statistical Institute stated that data on prices were not collected from earthquake-hit provinces.[9] Curiously, the fall in inflation delivered a welcome boost for the ruling party ahead of presidential and parliamentary elections in Türkiye.[10] The ruling party led by president Recep Tayyip Erdogan has won Turkey's presidential election which took place in May 2023. With that in mind, some economists have questioned Türkiye's official inflation rate statistics and suggested that the actual inflation rate might be have been higher. [11]

Before the war, during 2020 and the first half of 2021, **Ukraine** had one of the lowest inflation rates in the Black Sea region. In 2021 however, inflation in Ukraine substantially increased and hovered around 10% in the second half of the year. After Russia's invasion of Ukraine at the end of February 2022, inflation in the country rose further, and peaked at 26.6% in October 2022. Despite concerns about possible hyperinflation, the rate of inflation in Ukraine has remained under 30% since the beginning of the war.[12] Crucially, the inflationary pressures of the war in Ukraine have been kept down by state policies which have focused on shifting the burden of the war from businesses and the population to the budget through state support programs, freezing tariffs for the population, and fixing the Ukrainian Hryvnia exchange rate.[13] Notably, those state policies have been implemented with the support of international partners (partner countries, international organizations, donors) which have provided Ukraine with large financial and institutional aid to help the Ukrainian economy in maintaining the resilience during the wartime.[14] In March April 2023, inflation fell markedly to 21.317.9% from February's March's 24.921.3% as the country recorded its lowest inflation rate since May 2022. Among the main factors to have influenced the inflation slowdown were the stable energy supply[15], falling world fuel prices, and the policies of the National Bank of Ukraine, which had mainly refused to finance the budget deficit through printing money.[16]

Meanwhile in **Russia**, inflation soared to almost 18% following. its launching of war on Ukraine. Inflation in Russia has since been gradually stabilizing though and dropped to 11.0% by February 2023. In March, inflation sharply fell from 11.0% to 3.5%, going below the central bank's 4% target for the first time since the war began and wide-ranging global sanctions were imposed on the country.[17]

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7 https://www.economist.com/the-economist-explains/2022/01/27/is-recep-tayyip-erdogans-monetary-policy-as-mad-as-it-seems

8 https://english.alarabiya.net/business/economy/2023/02/03/Turkey-s-inflation-rate-slows-for-third-month-Data-

9 https://www.cnbc.com/2023/03/03/turkey-annual-inflation-dips-to-55point18percent-in-february.html#:~:text=Inflation%20has%20been%20stoked%20by,point%20cut%20following%20the%20earthquake.

10 https://jordantimes.com/news/business/turkeys-inflation-slows-further-presidential-vote-nears

11 https://www.barrons.com/news/turkey-s-inflation-slows-to-50-ahead-of-election-9b8a6bd7

12 First Deputy Prime Minister - Minister of Economy of Ukraine Yuliia Svyrydenko.

13 https://www.kmu.gov.ua/en/news/spozhyvcha-infliatsiia-za-pidsumkamy-2022-roku-stanovyla-266-tse-suttievo-menshe-prohnoziv

14 PMC Research, 2022. Economic outlook and indicators in Ukraine. Special Issue: Overview of the Measures Taken to Support the Ukrainian Economy During the War. https://pmcresearch.org/periodic_show/423/Special-Issue:-Overview-of-the-Measures-Taken-to-Support-the-Ukrainian-Economy-During-the-War

15 https://www.dw.com/en/how-ukraine-has-maintained-its-energy-supply-despite-the-war/a-65071162

16 Ukraine War Economy Tracker - Centre for Economic Strategy (ces.org.ua)

17 bloomberg.com/news/articles/2023-04-12/blamed-for-putinflation-abroad-russia-is-now-seeing-prices-dive#xj4y7vzkg

In April 2023, inflation further decreased to 2.3%. The low inflation can be attributed to several factors. Firstly, low inflation in Russia suggests that aggregate demand in the country remains low and that consumers are being careful in their spending as the war continues and the Russian economy remains affected by various sanctions. At the same time, the slowdown in inflation reflects a recovery in imports (Russian imports raised in Q1 2023[18]) and appreciation of ruble (in January-March 2023, the ruble's nominal effective exchange rate (NEER) was 26 % higher than in 2022). Notably, the sheer fall in year over year inflation rate does not indicate a real drop in prices in Russia, and could be mainly attributed to the base effect as inflation initially temporarily skyrocketed following the imposing of sanctions and the weakening of the Russian Ruble in March 2022. The prices remained high from March till May 2022, so stabilized later. Accordingly, from June 2023 inflation in Russia can be predicted to increase compared to previous months.

Bulgaria, having low inflation levels hovering at around 1% in 2020 and even recording deflation in the first months of 2021, has recorded a substantial rise in inflation starting in 2022. The global spike in energy and food prices following the war in Ukraine have substantially enhanced inflation in Bulgaria. Specifically, inflation peaked at 18.7% in September 2022, which was Bulgaria's highest rate since 1998.[19] and 5th highest rate of inflation in the European Union. In April 2023, Bulgaria recorded 11.6% YoY CPI inflation, the third highest among Black Sea countries after Türkiye and Ukraine. The primary reason for this is Bulgaria's high dependence on Russia's energy (prior to the war, 77% of gas in Bulgaria came from Russia[20]). Accordingly, it is predicted that as energy prices are decreasing, inflation in Bulgaria will also fall in 2023.[21]

Inflation trends in **Romania** for the analyzed period were similar to those witnessed in Bulgaria. Specifically, inflation in Romania accelerated from March 2022 with the outbreak of war in Ukraine and peaked at 16.8% in November 2022. Thereafter, inflation has slightly eased in Romania in 2023, declining to 11.2% in April. Moreover, through an extended government energy support scheme[22], inflation in Romania is expected to stabilize further.[23]

Following a global decline in inflation over the course of 2020, inflation in **Georgia** also fell markedly in the second half of 2020. In December 2020, inflation in Georgia dipped to 2.4% courtesy in large part to a major decrease (25.4 pp) in prices of "housing, water, electricity, gas and other fuels,"[24] which could be explained by the introduction of utility subsidies for households in November 2020.[25] Since the beginning of 2021, monthly YoY CPI inflation has been increasing sharply, surpassing pre-pandemic levels, and reaching a peak of 13.9% in December 2021. Throughout 2022, inflation in Georgia gradually decreased and then the drop accelerated in the first quarter of 2023, with Georgia reporting the lowest inflation rate in the Black Sea region during the first two months of 2023 (9.4% in January, and 8.1% in February). Though inflation in Russia was lower, Georgia's inflation continued to rapidly decline, amounting 5.3% in March 2023 and to 2.7% in April 2023. In May 2023 (the data for other countries of the region is not yet available for May 2023), inflation in Georgia reached as low as 1.5%.

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18 https://www.cbr.ru/eng/press/event/?id=14721#highlight=imports

19 https://china-cee.eu/2022/06/28/bulgaria-social-briefing-bulgarians-are-the-most-affected-by-the-rise-in-inflation-due-to-the-low-purchasing-power-of-the-population/

20 The European Union Agency for the Cooperation of Energy Regulators, 2020.

21 https://economy-finance.ec.europa.eu/economic-surveillance-eu-economies/bulgaria/economic-forecast-bulgaria_en

22 https://www.reuters.com/business/energy/romanias-government-extend-energy-support-bill-tax-entire-energy-chain-2022-09-01/

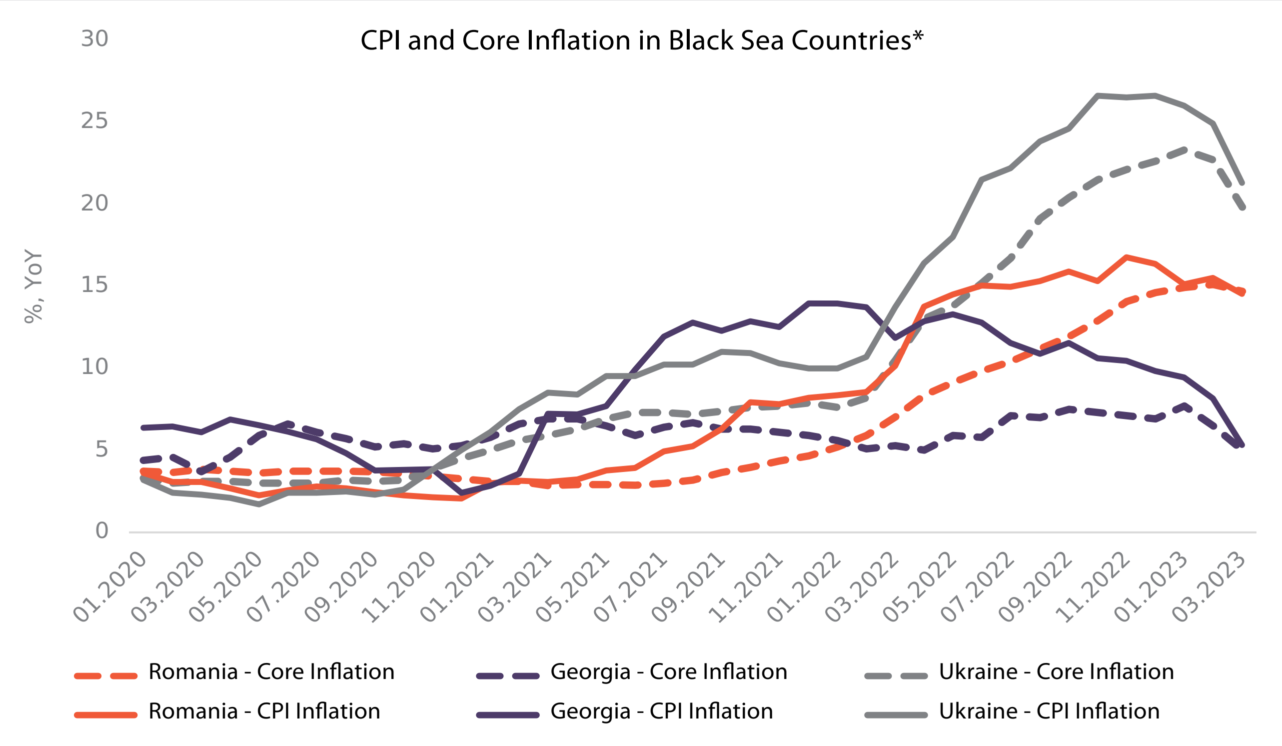
23 https://www.reuters.com/markets/europe/romanian-inflation-easing-not-within-target-by-2024-central-bank-2023-02-15/?fbclid=IwAR3RhwsbpkWFOmBqBwrVS9_H7U11skIqvWmjUKOYHBXnijlmXo4TA_ujSug

24 PMC Research, November 2021. Inflation Trends in Georgia. Economic Outlook and Indicators in Georgia.

25 https://matsne.gov.ge/ka/document/view/5026401?publication=0

CORE INFLATION IN BLACK SEA COUNTRIES

Graph 3



Source: Central banks of Black Sea countries

As Russia is a globally important energy exporter, and as Ukraine is one of the world's major grain producers, global energy and food prices have risen markedly with the outbreak of war, and these have played an important role in forming inflation trends thereafter. Thus, to gain a better understanding of inflation trends, it would be insightful to analyze core inflation data, which exclude the volatile energy and food components. According to the IMF, the recent decline in global inflation largely reflects the sharp reversal in energy and food prices, but core inflation is likely to be more persistent and will decline more slowly.[26]

From the Black Sea countries for which core inflation data were available[27], Georgia recorded the largest difference between core and CPI inflation. The difference peaked at 8.6 pp in February 2022, when Russia launched the war in Ukraine. In 2023, core inflation has moved closer to headline inflation in all analyzed Black Sea countries. In Romania, core inflation was 0.2 pp above headline inflation in March 2023 and experts expect core inflation to remain slightly above the headline rate for most of 2023.[28] This can be again explained by the above-mentioned energy support scheme introduced by the Romanian government, which has been holding down energy prices which are included in headline inflation calculations but excluded for core inflation.

Thus, interestingly, in the first quarter of 2023, only a small difference was recorded in Black Sea countries between core inflation, which excludes the volatile energy and food components, and headline inflation. In previous periods, the difference between core and headline inflation was more significant, implying that high headline inflation was being driven by high energy and food prices. In the first quarter of 2023, while headline inflation declined, core inflation remained high and close to headline inflation. Indeed, even though headline inflation declined, this was primarily due to the stabilization of volatile food and energy prices, and overall inflation remains high.

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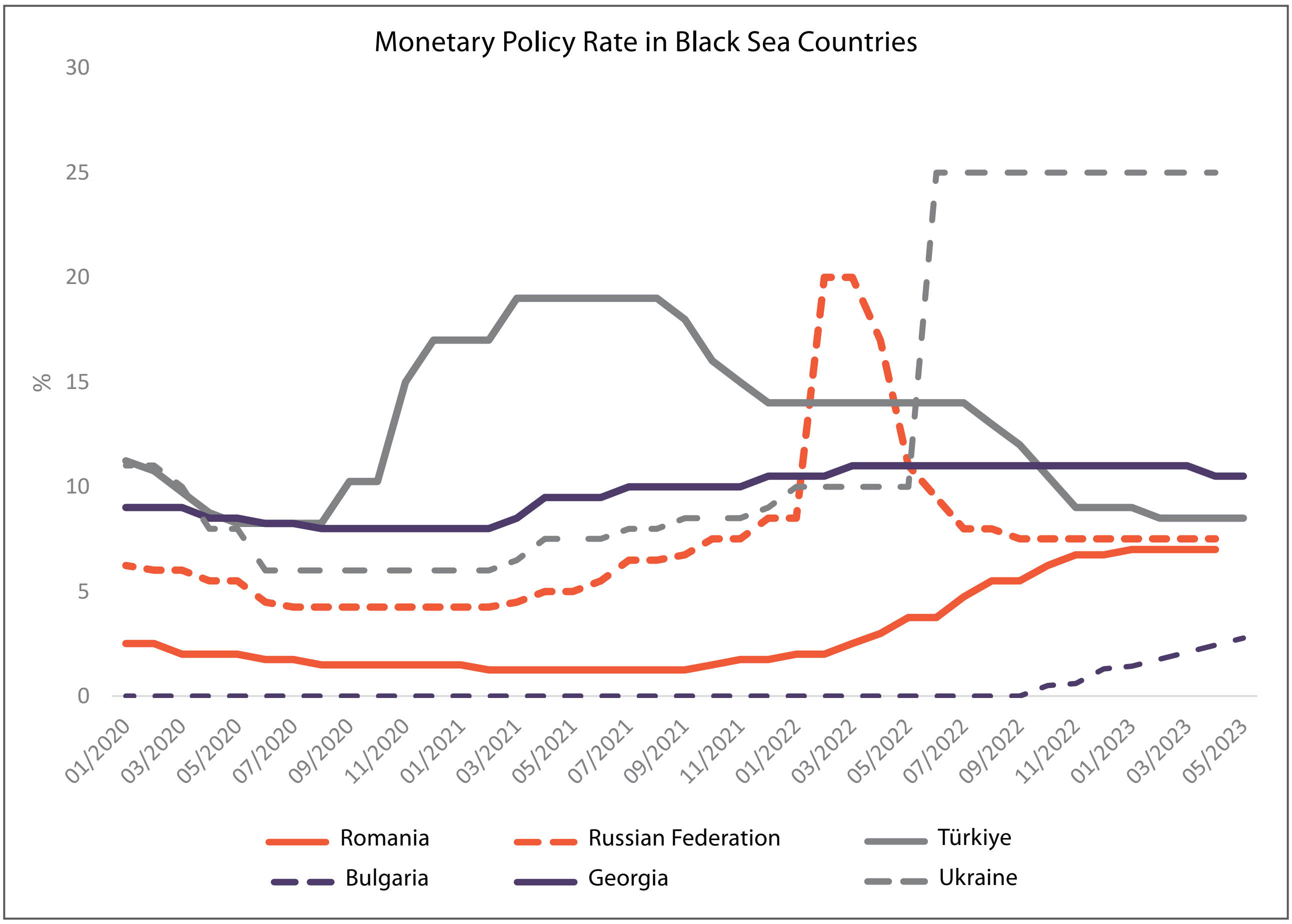
26 IMF, April 2023. World Economic Outlook. A Rocky Recovery.

27 To the best of the knowledge of authors, only data from Central Banks' of Georgia, Romania, and Ukraine were freely available/reported.

28 https://think.ing.com/snaps/romanian-inflation-continues-to-soften/

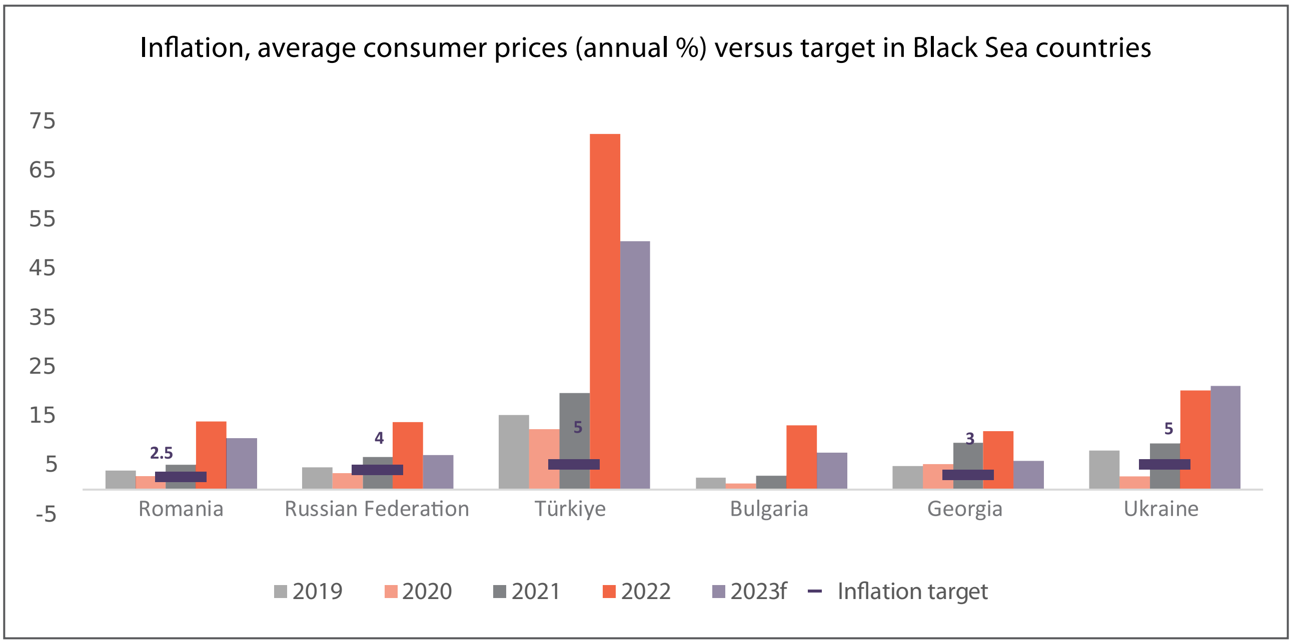
MONETARY POLICY IN BLACK SEA COUNTRIES

Graph 4



Source: Central banks of Black Sea countries

Graph 5



Source: IMF, World Economic Outlook Database

The central banks of Black Sea countries have conducted their monetary policies to address high and/or volatile inflation and its adverse effects on the economy. To control inflation, many central banks around the globe, including all Black Sea countries except Bulgaria, have been using a technique called "inflation targeting." Under inflation targeting, a central bank makes estimates and publicly sets a projected (or "target") inflation rate and then attempts to steer actual inflation toward that target.[29] The key instrument applied under an inflation targeting regime is the monetary policy rate. Specifically, central banks influence inflation by changing the monetary policy rate, as changes in the monetary policy rate affecting interest rate, credit, exchange rate, and expectation channels are reflected in aggregate demand and, ultimately, inflation dynamics.[30]

Ukraine currently has the highest monetary policy rate (25%) as well as the joint-highest inflation target (5%) among Black Sea countries. Decreasing its key monetary rate to 6% in June 2020 played a role in stimulating the economy and subsequently increasing inflation at the beginning of 2021. However, the inflation rate still overshot the target range in 2021 by 4 pp, which could be attributed to external price shocks and a low base effect. A few months after the beginning of the war, the National Bank of Ukraine postponed its monetary policy decision, though the key policy rate rose from 10% to 25% by 3 June 2022. Since then, the policy rate has remained unchanged. According to the current plans of the National Bank of Ukraine, this will continue to be the case at least until the end of the first quarter of 2024. In 2022, annual inflation in Ukraine was 20.2%, which is about fourfold its target.

Türkiye has the joint-highest inflation target in the region at 5%. In Türkiye, inflation targets are set jointly by the central bank and the Turkish government for three-year periods.[31] The inflation target of 5% in Türkiye has been unchanged since 2012, even though for the last few years inflation has been several times above the target. In 2022, annual inflation in Türkiye was 72%, which is about 14 times its target. Nevertheless, Türkiye underwent a series of monetary policy rate cuts in 2022. In February 2023, the central bank again cut the rate from 9% to 8.5%. Even though Ukraine has set the same inflation target as Türkiye and has much lower inflation, its central bank maintains a much higher monetary policy rate (about triple that of Türkiye). This helps Ukraine to maintain stable prices even in wartime.[32]

The inflation target in **Russia** is set at 4%. In 2022, when Russia launched its war against Ukraine and subsequently came under severe economic and financial sanctions, annual inflation reached 13.8%, which is 9.8 pp higher than its target. The Central Bank of Russia (CBR) immediately took measures in response to the impacts of war and sanctions and raised its monetary policy rate from 8.5% to 20% in February 2022. Throughout the year since, as inflation in Russia has stabilized, the CBR has also gradually reduced its policy rate. In September 2022, the monetary policy rate in Russia was set at 7.5% and it has been maintained at this level ever since.

Georgia has the highest monetary policy rate in the Black Sea region after Ukraine. From March 2022 onward, the National Bank of Georgia (NBG) had kept its policy rate at 11% but on 10 May 2023, the Monetary Policy Committee of the NBG announced the decision to reduce the monetary policy rate by 0.5 pp to 10.5%. The Committee reported that the reduction of inflation in Georgia had been supported by tight monetary policy and fiscal consolidation.[33] Moreover, it was stated that despite positive external factors putting downward pressure on inflation, uncertainty remained quite high

29 https://www.imf.org/external/pubs/ft/fandd/basics/72-inflation-targeting.htm

30 https://nbg.gov.ge/en/page/monetary-policy-rate

31 https://www.tcmb.gov.tr/wps/wcm/connect/EN/TCMB+EN/Main+Menu/Core+Functions/Monetary+Policy/PRICE+STABILITY+AND+INFLATION/Inflation+Targets

32 https://ces.org.ua/en/tracker-economy-during-the-war/

33 https://nbg.gov.ge/en/media/news/the-national-bank-of-georgia-keeps-its-monetary-policy-rate-unchanged-at-11-0-perce-7

due to the tense geopolitical situation. Thus, the NBG announced that, considering the high uncertainty and risks, it would remain focused on reducing inflation and maintaining a tight monetary policy. In 2022, annual inflation in Georgia was 11.9%, which is about 8.9 pp higher compared to its inflation target set at 3%.

Romania has the lowest inflation target (2.5%) in the region. In 2021, annual inflation in Romania was 2.5 pp above the target (at 5%), though in 2022 inflation escalated significantly beyond the target and reached almost 14%. Its central bank, which had been maintaining its policy rate at the second-lowest level in the region (after Bulgaria) – lower than 2% - before February 2022, has since gradually increased its rate in response to rising inflation. In January 2023, its central bank increased its policy rate to 7% and, despite inflation showing a slight easing, it kept the rate at 7% in following months (till April so far)..

Bulgaria is the only country in the Black Sea region which to not have adopted inflation targeting. Moreover, amid the rise in inflation, the role of Bulgaria's central bank in stabilizing inflation has been limited. The reason for this is that the implementation of monetary policy in Bulgaria is linked to that of the European Central Bank. While Bulgaria, despite being an EU member state for over 15 years already, has not adopted the euro as its currency and persists with the Bulgarian Lev (BGN). With an aim to join the Eurozone in the future, Bulgaria has however adopted the European exchange rate mechanism, meaning that the BGN is anchored to the euro.[34] Accordingly, the extent of monetary tightening has been much lighter in Bulgaria than in other countries in the region. The monetary policy rate in Bulgaria was maintained at 0% before October 2022, when it rose to 0.49%. Since then, the policy rate has been gradually rising and was set at at 2.77% in May 2023. Even though Romania, like Bulgaria, is also an EU member state which has not yet adopted the euro, the two countries have chosen diverging monetary policy paths since their EU accession. While Bulgaria has opted for a currency board arrangement that effectively eliminated the country's monetary autonomy, Romania has chosen to keep a more discretionary monetary policy regime.[35]

[34] https://economic-research.bnpparibas.com/html/en-US/Bulgaria-authorities-adopt-euro-2024-1/17/2023,48137

[35] Nenovsky, N., Tochkov, K., & Turcu, C. (2013). Monetary regimes, economic stability, and EU accession: Comparing Bulgaria and Romania. Communist and Post-Communist Studies, 46(1), 13–23. https://www.jstor.org/stable/48610370

CONCLUSION AND RECOMMENDATIONS

To sum up, inflation trends as well as monetary policy approaches widely vary among Black Sea countries. Türkiye stands out for its extraordinarily high level of inflation not only in a Black Sea region context, but globally. In April 2023, inflation in Turkey reached 43.7%, having earlier peaked at 85.5% in October 2022. The currency crisis (the steep depreciation of the Turkish Lira), the Turkish government's expansionary fiscal policy in tandem with a loose monetary policy have contributed significantly to high inflation in Türkiye. Meanwhile, the two Black Sea countries involved in the ongoing war – Russia and Ukraine – have recorded rather different inflation dynamics. While Ukraine also records high inflation – standing at 17.9% in April 2023 – the corresponding indicator for Russia has dropped to a relatively stable 5.3%. However, the low inflation rate in Russia should not be taken as a sign that the country is successfully dealing with the war and the sanctions imposed on it. On the contrary, the low inflation suggests that aggregate demand in the country remains low and consumers are being careful in their spending. Elsewhere, the war is cited as the main reason behind high inflation in the Black Sea region's two EU member states, namely Bulgaria and Romania which recorded YoY CPI inflation of 11.6% and 11.2% respectively in April 2023. At the same time, Georgia reported the lowest inflation in the Black Sea region during the first two months of 2023 (9.4% in January, and 8.1% in February), and this further declined to 5.3% in March 2023. Overall, inflation in Black Sea countries, in line with a global declining trend, dropped during the first quarter of 2023.

The Black Sea countries also widely differ in their monetary policy approaches implemented to tackle high inflationary pressures. In Türkiye, the central bank, going against traditionally accepted economic theories, has put in place a loose monetary policy rate in response to high inflation and has kept interest rates low. Türkiye undertook a series of monetary policy rate cuts in 2022. In February 2023, its central bank again cut the monetary policy rate from 9% to 8.5%. Meanwhile, in Ukraine, the central bank, with the same inflation target as Türkiye, has maintained a much higher (about three times higher) monetary policy rate (25%). Despite fighting a war, inflation in Ukraine has been lower than in Türkiye and the former has managed to maintain relatively stable prices. Russia's central bank has also actively used monetary policy rate as a tool to stabilize inflationary pressures stemming from the war and related sanctions. Bulgaria and Romania, both EU member states aspiring to join the euro area, have followed diverging monetary policy paths since their EU accession. Of note, Bulgaria has given up its monetary autonomy by anchoring its currency to the euro. As a result, its central bank has been limited in its usage of monetary policy tools to stabilize inflation, which has surged in the country since the beginning of the war. Meanwhile, Romania has gradually increased its monetary policy rate in response to rising inflation since February 2022. As a result, after the beginning of the war, inflation in Bulgaria was initially higher compared to Romania, though by April 2023, the pair had recorded almost the same inflation rate (11.6% and 11.2% respectively). Elsewhere, the National Bank of Georgia, with the second-highest monetary policy rate in the Black Sea region, actively utilizes a tight monetary policy rate to stabilize inflation in the country.

As described above, policymakers in Black Sea countries are taking different routes to address high inflation. So far, regardless of which policy approach has been applied, inflation remains well above the targets set for all countries of the region, albeit some have enjoyed greater success in stabilizing inflation than others. From the analysis of the policy approaches of Black Sea countries, it would seem prudent to suggest that central banks should **apply or maintain a tight monetary policy as a means of stabilizing inflation.**

At the same time, while tightening monetary policy, policymakers should **keep a focus on maintaining financial stability.** The recent failures of the regional banks in the US revealed that some banks were not sufficiently prepared to bear the stress of higher interest rates. Accordingly, while focusing on the goal of stabilizing inflation, central banks should also consider financial stability risks that might be implied. To maintain trust in the financial markets, policymakers can utilize tools such as imposing capital and liquidity requirements, risk monitoring, and prudential rules.

As, currently, financial systems face substantial uncertainty, it is also important that policymakers remain **flexible and independent, and able to adjust policies to rapidly changing demands.** Accordingly, it is important for central banks to stay independent and be capable of employing tools to both stabilize inflation and maintain financial stability. At the same time, keeping an independent monetary policy does not mean disregarding fiscal policy. On the contrary, an additional recommendation here is that monetary policymakers closely follow fiscal policy developments and try to employ complementary policies, or at least keep fiscal policies in mind while designing monetary policies.

Finally, it is crucial that central banks **clearly communicate their objectives and policy functions.** Indeed, maintaining confidence in central banks and policymakers is essential to maintain monetary and financial stability. Pertinently, the IMF announced: "If policymakers need to adjust the stance of monetary policy for financial stability purposes, they should clearly communicate their resolve to bring inflation back to target as soon as possible once financial stress lessens." It should also be noted that clear and timely communication of monetary policies would likely mitigate the emergence of high inflation.

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