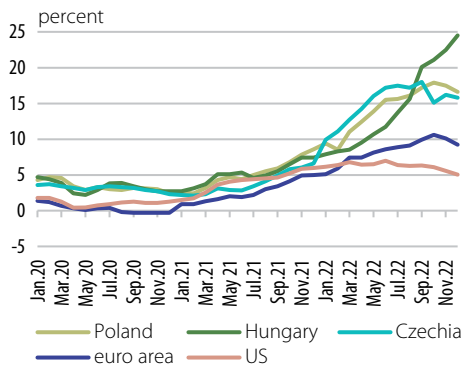
Box 4. The monetary policy stances of major central banks and of those in the region in 2022

The strengthening of global supply-side shocks under the impact of the war unleashed by Russia against Ukraine, but also the revival of consumer demand amid the lifting of anti-pandemic restrictions pushed the inflation dynamics even further above central banks' targets in 2022. This was the case both in emerging economies and in developed countries (Chart A), compounding at the same time the risk of de-anchoring longer-term inflation expectations, *inter alia* against the background of economic activity resilience and the almost across-the-board increase in labour market tensions.

Chart A
Annual inflation rates in the euro area, US and countries in the region



Note: The annual inflation rate is calculated based on national CPI (Czechia, Hungary, Poland), HICP (euro area) and seasonally-adjusted personal consumption expenditure index (US).

Source: Eurostat, national statistics institutes, FRED

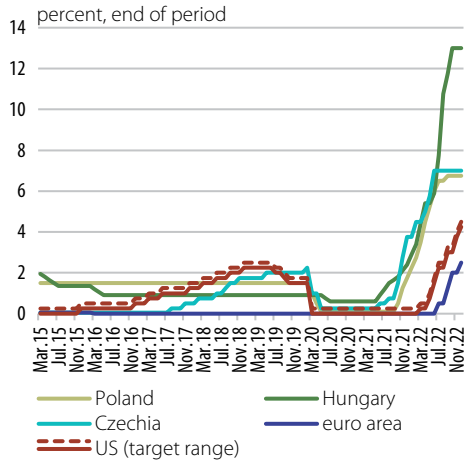
Central banks responded to this situation in a quasi-synchronised and unprecedented manner. Those in developed economies steepened markedly the normalisation path that the monetary policy stance had embarked on in 2021, while those in countries in the region hastened or extended the swift policy rate hiking cycle, by resorting to new exceptional increases in terms of magnitude and pace (Chart B).

Specifically, the ECB discontinued in March 2022 the net asset purchases under the pandemic emergency purchase programme (PEPP)[1], while at the beginning of July it also ended purchases under the asset purchase programme (APP), after having gradually reduced them during the first half of the year. At the same time, in June, the Governing Council decided and announced its intention to start in the following month and hasten afterwards the key rate hiking cycle, assuming the medium-term inflation outlook persists or deteriorates[2]. The approach was warranted by the strengthening, once with Russia's invasion of Ukraine, of the presumed impact exerted on inflation[3], but also on economic activity, by adverse supply-side shocks – mainly through higher energy prices, the disruption of international trade and weaker confidence –, as well as by the markedly higher uncertainties surrounding future developments.

1 In line with the December 2021 decision of the Governing Council.

2 Moreover, given the marked widening of some euro area sovereign spreads versus Germany, the Governing Council held an ad hoc meeting on 15 June, deciding to apply flexibility in reinvesting redemptions coming due in the PEPP portfolio, for preserving the functioning of the monetary policy transmission mechanism, and announcing the development of a new instrument meant to prevent euro area financial market fragmentation (Transmission Protection Instrument), which was then approved at the July meeting.

3 The ECB's March forecast anticipated in the near run strong inflationary effects from higher commodity prices, especially of natural gas and oil, but also modest disinflationary influences from the weakening of aggregate demand. Against this background, the average annual inflation rate was expected to pick up to 5.1 percent in 2022 (3.2 percent in the previous forecast), before returning in 2023 in line with the central bank's target (2.1 percent, only slightly above the previously-projected 1.8 percent). The forecasted levels of the annual inflation rate were again revised upwards in the June projection round, to 6.8 percent in 2022 and 3.5 percent in 2023.



Source: NCBs

Chart B
Monetary policy rate in the euro area, US and countries in the region

According to its announced intention, the ECB decided in July on the first policy rate hike since 2011, raising the three key interest rates by 0.50 percentage points, a larger step than signalled earlier[4]. Afterwards, it accelerated the hiking cycle, raising key rates by 0.75 percentage points in each of the September and October meetings[5] – the largest step from a historical perspective. The central bank's response was warranted by the further steep rise in the annual inflation rate – to a two-digit level in October (10.6 percent), mainly under the influence of higher energy and food prices –, as well as by the new sizeable upward revision of its anticipated path. The trajectory thus remained above the 2 percent target at the end of the projection horizon, even amid the significant deterioration of the economic growth outlook in the latter part of 2022 and in 2023 (Table A).

In December the ECB raised key rates by another 0.50 percentage points, thus increasing them by a total of 2.5 percentage points in the latter half of 2022[6]. Moreover, the Governing Council said that interest rates would still have to rise significantly at a steady pace to reach levels that were sufficiently restrictive to ensure a timely return of inflation to the target over the medium term. Also in December, it was decided that, from the beginning of March 2023 onwards, the APP portfolio would decline as the Eurosystem would not reinvest all of the principal payments from maturing securities[7]. The decisions were taken as the slight decrease in the annual inflation rate in November (to 10.1 percent)[8], after 16 months of steady rise, resulted entirely from lower energy price inflation, while underlying price pressures strengthened further and were expected to become more persistent. Therefore, the medium-term forecast of the annual inflation rate was again revised significantly upwards[9], even amid the worsening outlook for economic growth in 2023, *inter alia* in the context of a slight contraction anticipated in the short run, owing to the energy crisis, high uncertainty, and tighter financing conditions.

The Federal Reserve launched the key rate hiking cycle from the very first quarter of the year – earlier also vis-à-vis market expectations – and then accelerated the pace of monetary policy tightening. Specifically, the FOMC raised the target range

4 The deposit facility rate was raised to 0.00 percent, from -0.50 percent, the interest rate on main refinancing operations to 0.50 percent, from 0.00 percent, while the lending facility rate was increased to 0.75 percent, from 0.25 percent.

5 Also in October, the Governing Council changed the terms and conditions of the third series of targeted longer-term refinancing operations (TLTRO III) to ensure the consistency of this instrument with the monetary policy normalisation process. Thus, the ECB adjusted the interest rates on the operations from 23 November 2022, by indexing the interest rate paid to the average applicable key ECB interest rates, and offered banks three additional voluntary early repayment dates.

6 Hence, the deposit facility rate was raised to 2.00 percent, the interest rate on main refinancing operations to 2.50 percent, while the lending facility rate was increased to 2.75 percent.

7 The decline in the volume of holdings would amount to EUR 15 billion per month on average until the end of the second quarter of 2023 and its subsequent pace would be determined over time.

8 At the same time, the dynamics of its core component stood still at 5.0 percent.

9 Looking at the December projections, the average annual inflation rate anticipated for 2023 was revised to 6.3 percent (from 5.5 percent in the September round), while that for 2024 was revised to 3.4 percent (from 2.3 percent previously).

for the federal funds rate by 0.50 percentage points in May and by 0.75 percentage points at each of the June, July, September and November meetings, after having increased it by 0.25 percentage points in March[10]. In the closing month of the year, the central bank raised the target range for the federal funds rate by another 0.50 percentage points, thus bringing the total increase to 4.25 percentage points for the year overall, to 4.25-4.50 percent. In the context of the December decision, the Fed signalled its intention to extend the rate hiking cycle until the monetary policy stance becomes sufficiently restrictive to return inflation to 2 percent over time.

Table A. Macroeconomic developments and monetary policy stance in advanced economies and in the region

	Inflation target/ objective[b,c]	Annual inflation rate						Monetary policy rate[b,c]		Output gap[b,g]	General government balance, % of GDP				Current account balance, % of GDP			
		2022 (avg.)	2022 (end of period)	Forecast*[b,c]				Dec. 2021	Dec. 2022		2021	2022	Forecast*		2021	2022	Forecast*	
				2023 (avg.)	2024 (avg.)	2023 Q4	2024 Q4						2023	2024			2023	2024
Euro area	2 percent	8.4[a]	9.2[c]	6.3	3.4	3.6	3.3	0	2.5	marginally negative, slightly more negative values temporarily	-5.3[a]	-3.6[a]	-3.7[d]	-3.3[d]	2.3[d]	-1.0[d]	-1.4[c]	-1.0[c]
US	2 percent	6.3[f]	5.3[f]	3.1	2.5	-	-	0.00-0.25	4.25-4.50	quasi-nil gradually declining into negative territory and then progressively narrowing	-12.1[d]	-4.0[d]	-6.7[d]	-7.1[d]	-3.6[d]	-3.8[d]	-3.2[d]	-2.8[d]
Poland	2.5 percent ± 1 pp	14.3[e]	16.6[e]	13.1	5.9	8.0	4.9	1.75	6.75	marginally positive, on a decline and subsequent stay at mildly negative values	-1.8[a]	-3.7[a]	-5.5[d]	-5.2[d]	-1.4[a]	-3.0[a]	-2.5[d]	1.6[d]
Hungary	3 percent ± 1 pp	14.5[e]	24.5[e]	15.0-19.5	2.3-4.5	-	-	2.40	13.00	slightly positive, declining and then narrowing gradually	-7.1[a]	-6.2[d]	-3.5[b]	-2.5[b]	-3.9[a]	-8.2[a]	(-5.4)-(-4.2)[b]	(-2.8)-(-1.4)[b]
Czechia	2 percent ± 1 pp	15.1[e]	15.8[e]	9.1	2.4	4.2	2.4	3.75	7.00	negative and widening in the near run and gradually narrowing afterwards	-5.1[a]	-3.6[a]	-3.8[b]	-2.2[b]	-2.8[a]	-6.1[a]	-2.5[b]	-1.9[b]
Romania	2.5 percent ± 1 pp	13.7[e]	16.4[e]	-	-	11.2	4.2***	1.75	6.75	positive, narrowing	-7.1[a]	-6.2[a]	-5.0[d]	-4.8[d]	-7.2[a]	-9.3[a]	-8.8[d]	-8.4[d]

*) forecasted values refer to the latest central bank projections in 2022 and to the European Commission's autumn economic forecast (November 2022) respectively
**) calculated according to the ESA 2010 methodology
***) forecasted value corresponding to 2024 Q3
Sources: a) Eurostat, b) national central banks, c) ECB, d) European Commission (AMECO), e) national institutes of statistics, f) US Bureau of Economic Analysis, g) IMF

At the same time, the FOMC continued to implement during 2022 the plan for significantly reducing the size of the central bank's balance sheet. In particular, it decided to reduce again the monthly pace of financial asset purchases in January

[10] From 0.00-0.25 percent.

and to discontinue them in March, as well as to diminish holdings of Treasury securities and mortgage-backed securities starting 1 June 2022[11].

The decisions were taken in a context in which the annual inflation rate went up further in the first half of the year, peaking at a 40-year high[12], driven by costlier food and energy. Moreover, it stuck to high readings afterwards, albeit on a decreasing trajectory, reflecting the slower advance in energy prices, mainly due to the decline in crude oil prices, whereas opposite influences continued to stem from the swifter dynamics of food and services prices. At the same time, the labour market became extremely tight, amid the mismatch between the particularly solid labour demand and the slowly rising supply, which remained below pre-pandemic levels.

Against this background, the FOMC members' projections during the year pointed to a steady worsening of the inflation outlook, primarily over the near-term horizon to start with, and then in the longer run as well, implying a more sizeable and lengthier deviation of the annual inflation rate from the target. Furthermore, first-quarter assessments indicated that the unemployment rate would remain below the long-term equilibrium level throughout the projection horizon, whereas starting in H2 prospects emerged for a reopening of its positive gap as of 2023, also amid the adjustment of the monetary policy stance.

In the region, the Polish central bank continued to raise the monetary policy rate during the first three quarters of 2022[13], at a fast pace and with larger-than-standard increments. Specifically, the key rate was increased by 0.50 percentage points in January and February 2022 respectively, by 0.75 percentage points in March and by 1.00 percentage point in April, and then by 0.75 percentage points each time in May and June, 0.50 percentage points in July and by 0.25 percentage points in September, before being kept unchanged in Q4. During 2022 overall, the monetary policy rate was raised by a total of 5.00 percentage points[14], to 6.75 percent, while the deposit rate and the Lombard rate were increased in similar steps, to 6.25 percent and 7.25 percent respectively[15]. At the same time, the central bank announced and reiterated during the reported year the possibility of resorting to forex market interventions, especially with a view to moderating the zloty's exchange rate fluctuations inconsistent with the monetary policy stance.

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[11] In line with the *Plans for Reducing the Size of the Federal Reserve's Balance Sheet*, the volume of Treasury securities holdings was lowered in Q3 at a monthly pace of USD 30 billion, and then at a monthly pace of USD 60 billion. For mortgage-backed securities, the cap was USD 17.5 billion per month in Q3, increased afterwards to USD 35 billion per month. Thus, compared to June 2022, the total value of the Fed's financial asset holdings dropped by around USD 365 billion at end-2022.

[12] The CPI-based annual inflation rate climbed to 9.1 percent in June, from 7.0 percent in December 2021, while that calculated based on the personal consumption expenditure rose to 7.0 percent versus 6.0 percent at end-2021 (with the dynamics of its core component staying around the 5.0 percent level reached in December 2021).

[13] The central bank launched the rate hiking cycle in October 2021, increasing the monetary policy rate by 0.40 percentage points in October, 0.75 percentage points in November and 0.50 percentage points in December 2021, to 1.75 percent.

[14] In 2021 Q4, the central bank increased the policy rate by a total of 1.65 percentage points, starting from the historical low of 0.1 percent.

[15] The width of their corridor around the monetary policy rate was implicitly kept at ±0.50 percentage points.

The decisions were warranted by the strong pick-up in inflation during the first half of the year and by the marked deterioration of its outlook, under the impact of global supply-side shocks. Specifically, the annual inflation rate climbed to 15.5 percent in June, from 8.6 percent in December 2021[16] and, according to the July forecast, it was expected to remain on an upward path until 2023 Q1[17], before decreasing gradually, on a trajectory still above the target band until 2024 Q3. The inflation dynamics lost momentum in the second part of the year and even posted a downward adjustment at the end of the period under review[18]. The November projection reconfirmed the prospects for a decrease in the inflation dynamics after recording a peak in 2023 Q1, *inter alia* amid the widening of the negative output gap, given the likely decline in the pace of economic activity under the impact of weakening external demand and of the monetary policy stance adjustment.

In turn, the Czech National Bank continued to swiftly raise the monetary policy rate during the first half of the year[19], increasing it on four occasions during this period, in variable steps that cumulated 3.25 percentage points (0.75 percentage points in February and May, 0.50 percentage points in April, and 1.25 percentage points in June), up to 7.0 percent[20]. Moreover, at an extraordinary meeting held in May in response to the sizeable depreciation of the Czech koruna, the central bank's Board decided to make foreign exchange market interventions in order to prevent a longer-term weakening of the domestic currency[21], which could ease monetary conditions. The decisions were taken in a context in which the annual inflation rate had accelerated its increase in the first part of the year, also compared to forecasts[22], amid the strengthening of adverse supply-side shocks and the resilience of consumer demand, which brought about a marked worsening of the inflation outlook as well. Thus, the May macroeconomic forecast – updated after the outbreak of the war in Ukraine – saw the annual inflation rate pick up further until mid-2022 and then decrease on a significantly higher-than-previously-projected path[23], which remained above the target band at end-2023.

In the second part of the year, the central bank kept the monetary policy rate unchanged, in an environment marked by the slower rise in the annual inflation rate and its trend reversal in Q4[24]. Moreover, according to the November forecast, the inflation rate dynamics were expected to fall relatively swiftly in 2023 and decline to the vicinity of the midpoint of the target in 2024 H1. This was seen to

16 During the same period, the annual core inflation rate stepped up to 9.1 percent versus 5.3 percent.

17 Thus reaching 18.8 percent.

18 The annual inflation rate advanced to 17.9 percent in October, before slowing to 16.6 percent in December. Its core component climbed further during H2 overall, but more moderately, to stand at 11.5 percent in December.

19 The central bank started the policy rate hiking cycle in June 2021, raising the key rate five times in a row, from 0.25 percent to 3.75 percent in December 2021.

20 The deposit facility rate and the lending facility rate were raised accordingly, to 6.0 percent and 8.0 percent respectively.

21 In March, the central bank announced it conducted forex market interventions given the abrupt depreciation of the Czech koruna, amid financial market tensions entailed by the outbreak of the war in Ukraine. Moreover, it said that it stood ready to resort to additional interventions aimed at mitigating potential excessive fluctuations of the koruna's exchange rate, which might impair the smooth functioning of the financial market or jeopardise price stability and financial stability.

22 The annual inflation rate climbed to 17.2 percent in June, from 6.6 percent in December 2021.

23 Specifically, the average annual inflation rate forecasted for 2022 was revised upwards by 4.6 percentage points against the February projection, to 13.1 percent, while that for 2023 by 1.8 percentage points, to 4.1 percent.

24 The inflation dynamics peaked at 18.0 percent in September.

occur amid the moderation of cost increases, but also the slowdown in economic growth and the probably temporary contraction of economic activity – following the weakening of external demand and the tightening of monetary policy in previous quarters –, implying the output gap becoming and subsequently remaining negative. The monetary authority extended, however, its commitment to acting with a view to preventing excessive fluctuations of the koruna's exchange rate.

The Hungarian central bank resorted to a considerably larger increase in interest rates during 2022, given the relatively more pronounced deterioration of inflation developments and its outlook[25], but also the lingering tensions on the domestic financial market, resulting in the significant – and temporarily abrupt – weakening of the domestic currency. Specifically, the central bank raised the monetary policy rate at a faster pace both January through May, when it conducted five increases, in steps of 0.5 percentage points and 1 percentage point[26,27], and June through September, when it resorted to five new upward adjustments, in steps of up to 2 percentage points[28]. Consequently, the monetary policy rate was raised during the first three quarters overall by a total of 10.6 percentage points, to 13.0 percent[29]. The central bank also increased during 2022 the interest rate on 1W deposits, the main monetary policy instrument used in this period, more moderately in H1 – in order to become gradually realigned with the monetary policy rate after its more sizeable adjustment at end-2021[30] –, but in tandem with the latter subsequently.

At the onset of Q4, during an extraordinary meeting warranted by the strengthening of depreciation pressures on the forint, the Monetary Council adopted several measures, including the launch of overnight deposit quick tenders on a daily basis (which became the main monetary policy instrument[31]) at an interest rate of 18.0 percent, as well as the 9.5 percentage point increase in ON and 1W lending rates, to 25.0 percent[32]. Afterwards, the central bank kept unchanged the parameters of monetary policy instruments.

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25 The step-up in the annual inflation rate accelerated throughout the year, with inflation reaching 24.5 percent in December 2022 from 7.4 percent at the end of the previous year. During the same period, the core component dynamics rose to 24.8 percent, versus 6.4 percent, while inflation prospects successively deteriorated markedly. Thus, the December forecast saw the annual inflation rate pick up further over the winter months, before declining and returning in 2024 inside the 3 percent ±1 percentage point target band, amid the slower growth of domestic economic activity, the monetary policy measures adopted, as well as some strong base effects. Hence, the average inflation rate was envisaged to range between 15.0 percent and 19.5 percent in 2023 and between 2.3 percent and 4.5 percent in 2024.

26 The central bank raised in similar steps the deposit rate (which was brought, starting December 2021, to the same level as the monetary policy rate), but increased in March by 1 percentage point more the overnight and one-week lending rates, whose spread versus the monetary policy rate was thus widened to 3 percentage points.

27 In addition, in April, the central bank announced the end of the Bond Funding for Growth Scheme.

28 In June, the 1.85 percentage point hike in the monetary policy rate was accompanied by a smaller increase (1.35 percentage points) in the deposit rate and in the ON and 1W lending rates. Hence, the central bank reinstituted the interest rate corridor (width of -0.50/+2.50 percentage points around the monetary policy rate), after having brought the level of the deposit rate on par with that of the policy rate in December 2021.

29 The central bank had embarked on the policy rate hiking cycle in mid-2021, increasing the monetary policy rate June through December 2021 to 2.4 percent from 0.6 percent.

30 In the period from November to December 2021, the interest rate on 1W deposits was raised by 2.20 percentage points (the 0.7 percentage point and 0.4 percentage point rises decided in the latter half of November were followed by 0.2-0.3 percentage point increases over the following weeks), while the monetary policy rate was raised by 0.6 percentage points.

31 As of 13 October, the central bank no longer held 1W deposit-taking weekly tenders, with excess liquidity in the banking system being mopped up afterwards primarily via the new overnight deposit quick tenders and, to a smaller extent, through one-day (T/N) foreign exchange swaps (whose interest rate was raised by 4 percentage points, to 17.0 percent), as well as via longer-term (up to six months) deposit-taking operations.

32 The amplitude of the top of the interest rate corridor was implicitly broadened to 12 percentage points.