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Nowcast of the Annual Change in Real GDP for the Second and Third Quarters of 2023 and Inflation in the Short Term

Continuation of inflation slowdown in the third quarter of 2023

Sarajevo, 25 September 2023



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Key notes:

- *We nowcast the annual growth of real GDP for the second quarter at 0.8%.*
- *Despite the expected growth of activity in the service sector, especially the tourism sector, being more significant than expected slowdown in inflation, economic activity in the third quarter is expected to remain relatively muted, following an increasingly pronounced decline in demand. The preliminary nowcast of real GDP growth in the third quarter is 0.9%.*
- *We expect that inflation in the second half of the current year will be significant, but much lower compared to the first half of the year. Most of the inflationary pressures is, at the moment, consequence of the increase in domestic prices, which are not influenced by the increase in food and energy prices on the foreign market.*
- *Official statistical data for June and July indicate an unexpectedly strong slowdown in inflation, which resulted in a relatively significant revision of the estimate of core and headline inflation in the short term. In this round of inflation nowcast, we project that core inflation could be 6.0% and headline inflation 4.0% in the third quarter.*
- *The preliminary estimate of total inflation for the fourth quarter is 3.5%.*

Based on available official statistical data and information from international markets published until September 11, the Central Bank of Bosnia and Herzegovina (CBBH) estimates the annual growth of real GDP in the second quarter of 2023 at 0.8%, which is identical to the previous estimate from June, when we had high frequency data for April.

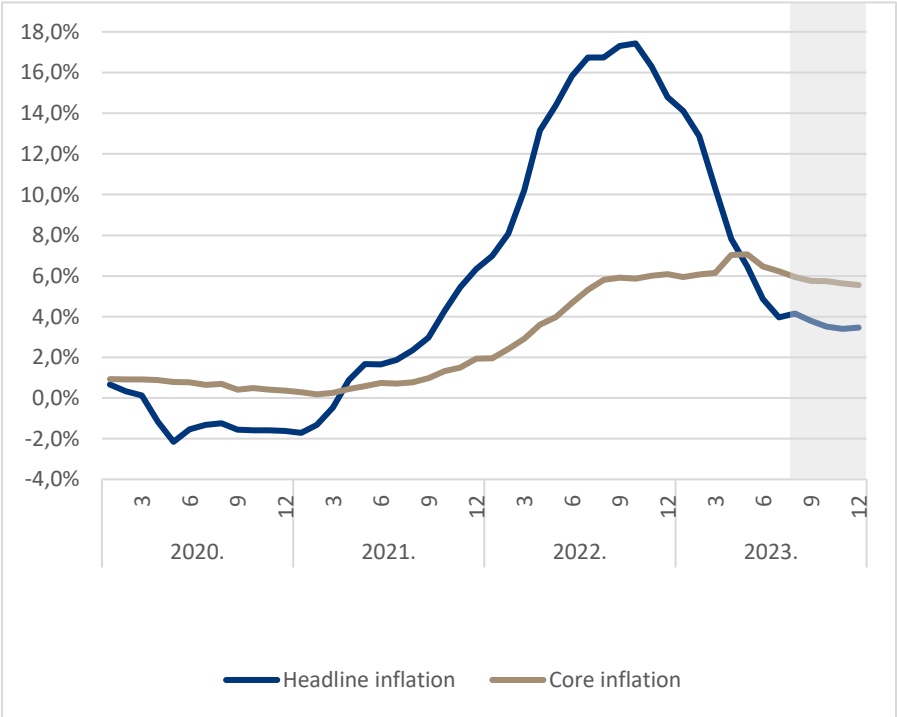
We forecast that the service sector, primarily activities related to tourism, made a significant contribution to economic activity in the third quarter. Consequently, and in the context of weakening inflationary pressures, we estimate slightly higher real GDP growth in the third quarter compared to the previous quarter. Bearing in mind that the downward trend of the industrial production and exports, on an annual basis, continued in July, it is certain that the trend of modest economic activity will continue in the third quarter, as well. Our first nowcast of annual real GDP growth in the third quarter is 0.9%. If personal consumption and export of services do not compensate for the fall in external demand in the remaining two months of the third quarter and in the last quarter, in the autumn round of medium-term macroeconomic projections, it is very certain that the real economic activity for 2023 will be corrected downwards compared to the spring round. In the spring round of medium-term macroeconomic projections, we announced that in 2023 we expect modest real GDP growth of 1.6%.

Our nowcast points to an easing of inflationary pressures. Nevertheless, we expect that inflation in the short term will continue to be significantly higher than the average for the period since official data on consumer prices in BH have been compiled. Officially published inflation in Bosnia and Herzegovina, of only 4% in July, indicates an unexpectedly rapid slowdown in inflation. Average price growth observed by the Entities is significantly different. According to the data of Entities' Agencies of Statistics, in July, annual inflation of 5.2% was recorded in Republika Srpska, while inflation of 2.8% was recorded in the Federation of Bosnia and Herzegovina, according to which this inflation rate is by far the lowest in the region. The significant slowdown in inflation, according to official data, in June and July resulted in a downward revision of our estimates related to inflation in the second half of the year.

We currently estimate that the annual growth of average consumer prices in the second half of the year could amount to 3.7%. Based on a preliminary estimate of price components for the remaining five months of the current year, we project that core inflation could be 6.1% and headline inflation 6.4% in 2023. In the spring round of medium-term macroeconomic projections of the CBBH,

inflation of 7.7% for 2023 was projected, i.e. 1.3 percentage points more compared to the current forecast from this reporting period. Inflation in Bosnia and Herzegovina is currently primarily effected by changes in the level of core inflation, which excludes the prices of food, alcoholic beverages and tobacco, as well as energy, which indicates an continuously higher increase in domestic prices. The utilities section has an increasingly significant impact on domestic inflation, primarily due to rising gas prices, rents and utility costs. In addition, electricity prices, as the most important subsection of total utility costs, recorded a significant increase (6.8%) in the first seven months of the current year, while their impact on inflation last year was insignificant. The rise in electricity prices, along with the already present increase in the prices of oil and oil derivatives, may further increase inflationary pressure in the coming period.

Graph 1: Projections of Headline and Core Inflations in BH



Source: BHAS, CBBH.

Note: The calculation and estimate of core inflation in BH relies on a methodology that excludes: 01 Food and non-alcoholic beverages, 04.05.02 (Gas), 04.05.03 (Liquid fuels), 04.05.04 (Solid fuels), 04.05.05 (Heat energy), and 07.02.02 (Fuels and lubricants). Core inflation, as of July 2023, is an estimate of the CBBH based on official historical data published by BHAS.

The publication of the results of the next round of medium-term macroeconomic projections for the period 2023-2025, with the revision of the annual projections of key macroeconomic variables for 2023 and 2024, is planned for November 2023. We plan to publish the next round of nowcast on the GDP and the headline and core inflation at the end of 2023.