National Bank of Romania changes rhetoric

Even though the change in tone is significant, the minutes hardly back any imminent action at the next meeting

Source: istock

Economic overview

The most important change is the assessment of the risks to the inflation outlook from 'relative equilibrium, except for electricity' to 'tilted to the upside'. However, this is largely viewed to be driven by 'administered and fuel prices', whereas a lower than previously anticipated contribution is seen 'especially from core inflation'.

At the same time, GDP growth in 3Q17 is seen 'markedly faster-than-previously forecasted in annual terms' despite an expected sequential slowdown. Another change in the assessment of the current account deficit from 'without being threatening yet' is to 'worrisome, inter alia in terms of the leu exchange rate developments'. Real monetary conditions are still being labelled as 'highly accommodative'.

On the fiscal outlook, the National Bank of Romania (NBR) minutes see the expansionary plans 'potentially alleviated however by the accompanying fiscal measures' and mention 'the possibility of further corrective fiscal measures in the context of defining the outline of the 2018 budget'. No

reference is made anymore to the 'conduct of other central banks in the region' or the ECB's stance and outlook.

Liquidity shortage drives interest rate spike

Apart from higher inflation expectations and pricing-in policy tightening, the NBR considers the recent spike in interest rates received a 'significant impetus' from 'the reduction in the structural liquidity surplus on the money market, under the simultaneous influence of the key autonomous liquidity factors, with a major role played by the operations in the Treasury account' and NBR FX interventions due to outflows from international investors likely due to a 'shift in the related risk perception'.

In our view, the NBR move was rather reactive, as the liquidity picture changed from a surplus to deficit

The liquidity shortage is expected to last a bit longer than 'the occasional ones emerging at the onset of a new reserve maintenance period' but is seen 'nevertheless temporary in nature, given the highly likely significant easing of the budget execution in the latter part of the fourth quarter'.

Marginal tightening from NBR

The NBR Board voted 8-1 to narrow the standing facilities corridor from ±150ppt to ±125ppt. This is a marginal tightening. One member voted to cut the RRR for RON liabilities, an easing measure.

In our view, the NBR move was rather reactive, as the liquidity picture changed from a surplus to deficit and the higher deposit facility rate would become effective only when the liquidity turns to surplus again, likely towards the end of the year.

40% November corridor narrowing probability

ING Forecast

No imminent action likely from NBR

The change in rhetoric is significant, especially on the risk balance to the inflation outlook and current account assessment, but the minutes don't suggest imminent action through further narrowing the standing facilities corridor at the next meeting on 7 November.

Such a move was mentioned by the NBR governor at the press briefing. Still, another narrowing of the standing facilities corridor at the next meeting might also have no immediate impact on the policy stance as a liquidity shortage is likely to persist.

A decision to narrow the corridor in November by another 25bp might be a function of FX pressures. With fiscal uncertainties unlikely to be out of the picture by then, we attach a 40% probability to such a move, while keeping our base scenario unchanged. This envisages 25bp of

normalisation/tightening each quarter (via narrowing the corridor and/or hiking the key rate) until 4Q18.