# Romania: Peak inflation?

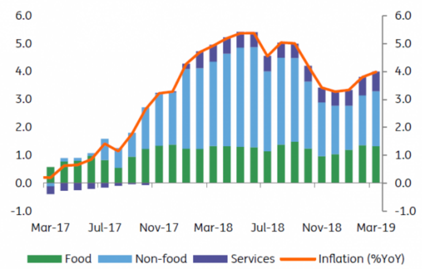
March CPI inched 0.2 percentage points higher to 4.0% year-on-year, above our forecast and the Bloomberg median of 3.9%. This is likely to be the peak for inflation this year

People on Calea Victoriei, Bucharest

## Volatile food prices

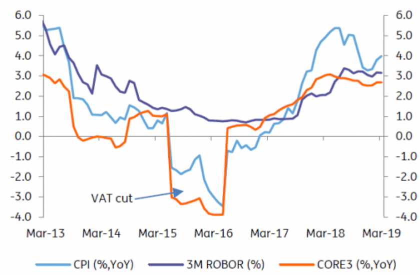
Core CPI was flat at 2.7% YoY, in line with our expectations. The surprise to our forecast for headline inflation came from volatile food prices. Food prices were flat at 4.5% while non-food CPI spiked 0.4ppt higher to 4.2%, mainly driven by higher oil prices. Services inflation rose 0.1ppt to 3.2% YoY.

**Fig 1 Broad based inflationary pressures**




Source: NIS, ING

**Fig 2 Core inflation stable, below relevant interest rates**




Source: NIS, NBR, ING

## Risks to the upside

At 4.0%, inflation is likely to have peaked this year, assuming no meaningful supply shocks ahead (including from regulated prices), though it could get close to this level towards the end of the year. We see year-end inflation at 3.8%, with the risk tilted to the upside. The fragile currency fundamentals remain the main medium-term threat to inflation and inflation expectations.

The National Bank of Romania is likely to try to manage the currency for a while to keep inflation expectations in check, allowing real effective exchange rate depreciation within the limits of inflation differentials, by maintaining the prohibitively high cost of carry combined with FX interventions. At the same time, the key rate is likely to stay flat at 2.50%. The credit facility rate of 3.50% is likely to remain the relevant instrument for policy implementation due to “strict" liquidity management, though key rate hikes should not be ruled out. In this context, a further deterioration of the trade balance is likely given the loose fiscal and income policies. Hence, a depreciation in the Romanian leu has merely been postponed.