National Bank of Romania review: Pushing through the policy space

The National Bank of Romania (NBR) has decided on a second consecutive 25bp rate cut to 6.50%, motivated by the recent reduction in inflation and its downwardly revised forecasts which opened up some policy space. In this context, additional rate cuts cannot be excluded in 2024, but absent further downside surprises in inflation, this is not our base case

Mugur Isarescu, Governor of the Romanian National Bank

The NBR's decision to deliver a second consecutive cut came on the back of recent inflation data, which brought some fairly decent policy space with it. Moreover, the Bank looks fairly optimistic regarding the disinflation trajectory further on (more details on that on Friday at the presentation of the August Inflation Report). If that is the case, the policy space arguments should allow for some further small cuts. The latest communique tends to suggest that the Bank places more emphasis on acting on a window of opportunity brought chiefly by the latest inflation prints, despite the lingering medium-term risks. This is not to say that medium-term risks stemming from strengthening internal demand, double-digit wage growth and fiscal policy are not on the Bank's radar. Rather, it seems that the Bank calibrated its policy with less weight on them at this stage than we had initially expected. The international rates context might have also mattered, with the growing probability that the Federal Reserve will deliver a series of rate cuts as of this autumn, which will make the European Central Bank's life easier in cutting as well.

Looking ahead, we continue to think that the NBR's monetary stance is unlikely to get too loose too soon. As we have mentioned in the past, the reasons for the recent progress on the inflation front are not necessarily due to factors that are under the NBR's control, like some of the food prices which are strongly influenced by international developments and energy prices influenced by local regulation. On that note, there seems to be more work to be done to moderate internal demand pressures, especially when we look at credit activity, retail sales and wage growth. The two recent consecutive cuts are not helping in this direction and might require stricter policy restrictiveness in the medium term.

All told, unless inflation continues to consistently surprise to the downside, policymakers' ability to capitalise on short-term gains from factors which are not necessarily under their control is unlikely to last forever. In the end, the economy's fundamentals and the sources of risks will likely have to dominate the policy optimisation, potentially more than they did at this decision. At the same time, if we were to follow the arguments for today's rate cut, the policy space to cut further might be even bigger at the next meeting, as inflation should be visibly lower by October, increasing real positive rates. For now, we nevertheless expect the key rate to remain at 6.50% until the year-end, as the Bank will likely want to see a consolidation of the disinflationary trend and not only one-off factors pushing the headline rate below expectations.

Authors

Stefan Posea
Economist, Romania
tiberiu-stefan.posea@ing.com

Valentin Tataru
Chief Economist, Romania
valentin.tataru@ing.com