

National Bank of Romania set to remain cautious this year

The National Bank of Romania (NBR) kept the policy rate on hold at 6.50% on 14 February. Today, while presenting the quarterly inflation report, Governor Mugur Isarescu hinted that rate cuts or FX depreciation are not on the table until internal and external risks moderate. We still think that rate cuts are possible in the second part of the year



Mugur Isarescu,
Governor of the
Romanian National
Bank

The NBR's decision to keep the key rate unchanged was influenced by multiple factors related to both the internal and the external environment. Domestically, policymakers hinted yet again that more fiscal clarity is needed. This would likely stem from the evolution of the ongoing budget execution until summer, as well as the potentially new fiscal measures further down the line this year.

Externally, Governor Isarescu indicated that the Bank's projections take into account a "reasonable" scenario stemming from the US tariffs situation and its impact on Europe. Moreover, he pointed out very high uncertainties regarding the risks to the Bank's latest inflation outlook coming from the ongoing and potentially rapidly changing geopolitical situation.

Some room to continue the rate-cutting cycle could be envisaged

Proceeding with policy easing given the current external imbalances is perceived by policymakers as an amplification of the current financial stability risks, and it could be perceived by markets “as an invitation towards currency devaluation”. Isarescu mentioned today that the NBR would not be happy with such an outcome.

But, in our view, a further depreciation of the RON, in a smooth and controlled manner, likely remains on the cards if a window of opportunity emerges later in the year.

Key to remember is that the necessary conditions for further rate cuts and a return to the previous trend of controlled FX depreciation seem pretty much aligned, namely growing confidence in the inflation outlook stemming from both the fiscal impulse and private consumption behaviour, as well as from lower external uncertainties.

Our forecasts and the outlook

On the inflation outlook, we expect CPI to end this year at 4.8% (1pp above the NBR's upwardly revised 3.8%). Our forecast takes into account strengthening food inflation further down the line, accounting for a large chunk of the upside pressures. Moreover, we think that both non-food and services inflation are set to decelerate only slowly and remain relatively sticky in the short to medium term.

We continue to expect two rate cuts amounting to 50bp from the NBR this year but starting from the second half of the year at the earliest. On FX, our base case remains for a small depreciation towards the year-end, taking the EUR/RON pair to 5.05

However, given all of the uncertainties, we think policymakers will need an even stronger conviction in their outlook compared to previous policy easing decisions, which keep risks for rates alive. Overall, we think that even if the Bank's negative scenarios on private consumption and aggregate demand were to materialise, as long as fiscal uncertainty persists, the bar for further rate cuts will remain quite high.

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