Romania and quantitative easing, who would've thought...

Following today's decisions, monetary policy is entering a new phase in Romania. We expect a significant downward adjustment in rates and increased pressures on the currency

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The National Bank of Romania announced today a package of measures "aimed at mitigating the impact of the situation generated by the coronavirus outbreak on households and Romanian companies". The Board meeting was an extraordinary one. These decisions are:

- The policy rate was cut 0.50 percentage points, from 2.5 percent to 2.0 percent
- The symmetrical corridor defined by interest rates on standing facilities around the monetary policy rate was narrowed to ±0.5 percentage points from ±1.0 percentage points
- Credit institutions will receive liquidity via repo transactions
- Leu-denominated government securities will be purchased on the secondary market

Today's decision was definitely unexpected by most – if not all – analysts. It follows similar measures taken by other central banks in the region (e.g.Poland, Czech Republic, Hungary, Serbia, Croatia). From the set of measures taken, we have already envisaged liquidity injections, one-to-two rate cuts in the second part of the year, plus minimum reserve cuts.

The most surprising and powerful detail of the decision (and the one we are lacking any details so far) is undoubtedly the intention to buy bonds from the secondary market. It is a first such step for the NBR, and it signals an important shift in its so far relatively strict inflation-targeting stance, by extending the range of policy tools the central bank can use. The details on how this programme will work and about the value of purchases are eagerly expected by the markets. The measure will likely unfreeze the situation on the fixed income market where long-term yields have been reaching above 6% levels in the last days and the Ministry of Finance had a series of unsuccessful auctions. It most likely comes to support the increased issuance needs of the Ministry of Finance in the upcoming months, as the economy is bracing for a serious contraction. Hence, although we don't have any details yet, it is difficult to imagine anything but a positive price action in the bond market. We tend to believe that the front end of the curve will be more favoured due also to the lower carry.

The press release mentions also that "the main ROBOR rates are expected to witness a significant downward adjustment" as a consequence of narrowing of the corridor around the key rate. A common-sense estimate in this respect is that the move in Robor rates will roughly reflect the 100bp cut change in the Lombard rate (which was cut from 3.50% to 2.50%).

Worth mentioning as well that the NBR decided to officially go into some sort of "crisis-management mood" by suspending the previously announced calendar of policy meetings and just hold them whenever it is considered necessary.

On the currency side, the depreciation pressures on RON will likely increase on the back of lower carry rates and improved liquidity. However, the NBR has repeatedly proven that is able to smooth the volatility and steer the currency. We expect stability on the FX front for the days to come, until the market will have more details on NBR's bond purchase intentions.

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