Romania: Inflation back within target. Who'd have thought?

After reaching a high of 5.4% in mid-2018 and staying above 4.0% for most of the year, the inflation rate has fallen within the central bank's target, to 3.3% in December 2018

The National Bank of Romania building in Bucharest

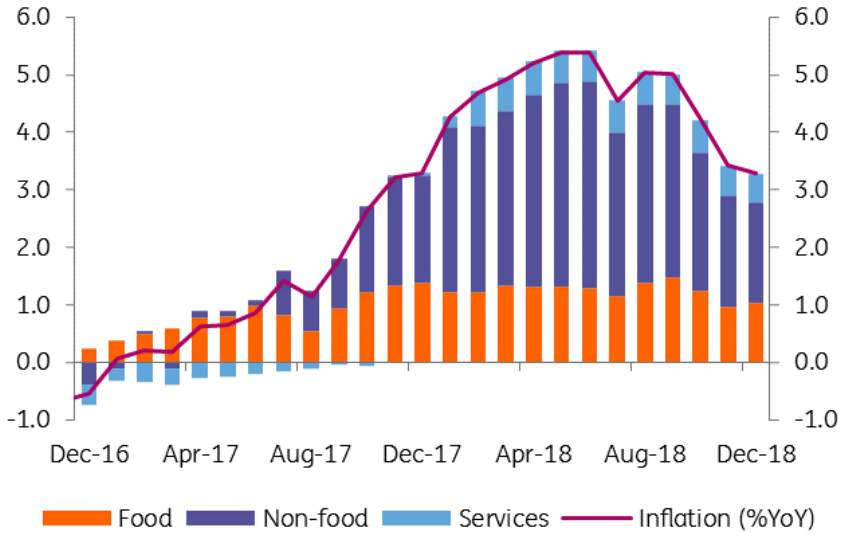
Source: Shutterstock

Greatly helped by the drop in oil prices towards the end of 2018 but also by the "careful calibration of monetary policy", the central bank managed to bring inflation back within its 2.5%±1ppt target band. Inflation declined in line with market expectations to 3.3%in December 2018 compared to December 2017 and marginally above our 3.2% call. Core inflation remained quite well behaved and came in line with our estimates, at 2.5%.

Food prices accelerated slightly from 2.9% in November to 3.1%, with vegetables posting a 22% increase while fresh fruit prices declined by 8%. This added c.1.1 percentage points to the total 3.3% December CPI.

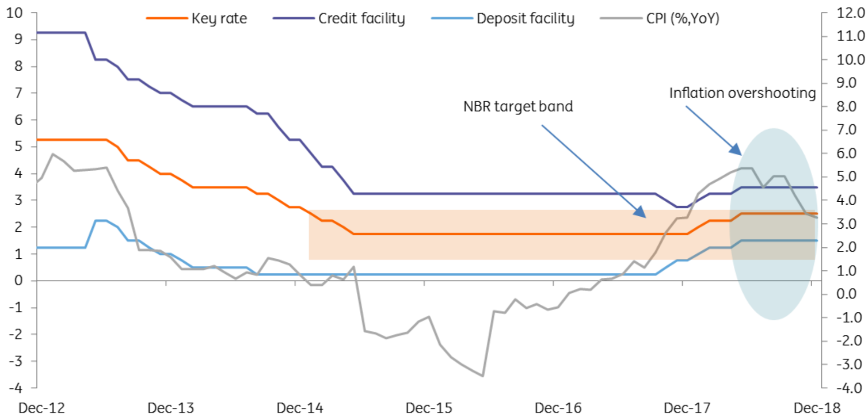
Inflation for non-food items reached 3.8%, its lowest in 2018, mostly on lower oil prices. Higher tobacco prices partly offset the lower fuel price, but the non-food items contribution to total inflation still declined to c.1.7 percentage points from 1.9 in November. CPI for services reached 2.4% from 2.5% in the previous month.

Inflation breakdown



Source: NIS, ING

Back to target



Source: NIS, NBR, ING

Oil prices aside, the 2018 inflation performance still looks impressive. Moreover, it was achieved with fewer hikes than the market was pricing although to some extent, this came at the expense of the exchange rate, as the Romanian leu appreciated in 2018 in relative terms versus most of its regional peers, thus putting pressure on an already negative trade balance.

The market is likely still assessing the impact of recent fiscal measures while more clarity on the budget draft for 2019 is expected, with parliament likely to vote on the budget bill in early February. Depending on the final form of these measures and the 2019 budget bill, the “careful calibration of monetary policy” could need even more scrupulous fine-tuning in 2019. We currently forecast only one ECB-dependent hike in 2019 from the National Bank of Romania, but risks are skewed to the downside.

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