Romania: Lower CPI, wider trade deficit

June CPI came in 0.3ppt lower at 3.8% YoY vs the Bloomberg median and ING estimates of 4.0% and 3.7% respectively. The good news ends here. Consumers bouyed by strong wages and accommodative policies have pushed core inflation to eight year highs and the trade gap to -3.0% of GDP, the widest in ten years for the January-May period

Source: Shutterstock

Food inflation inched 0.2ppt lower to 5.0% YoY in June. Non-food price inflation come down by 0.4ppt to 2.9%, driven by oil. Prices for services stood flat at 4.3%. Core inflation inched 0.1ppt higher to 3.3% YoY, nearing the upper bound of the NBR target band, and reflecting quite strong underlying inflationary pressures. From this perspective it looks like the NBR dropped the commitment to strict liquidity management a bit too early. This was likely driven by external factors which, among other things, has led to RON strengthening.

3.8% YoY

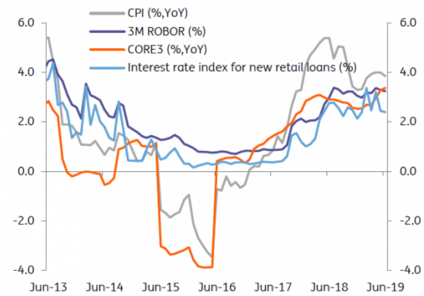
June CPI

ING forecast at 3.7%

Lower than expected

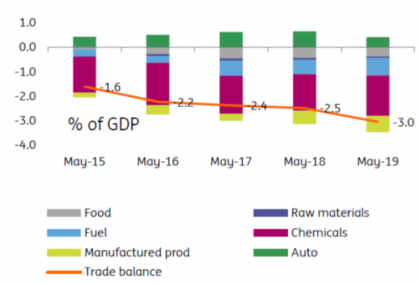
At the same time, the deterioration of the trade balance - which widened by 30% YoY in January-May versus the same period of 2018 - is supporting the NBR policy of fending-off RON appreciation via lower market rates and FX interventions. The deterioration of the trade deficit was broad-based, with the gap on both fuel and manufactured products widening by 28%, while the surplus on the auto segment shrink by 32%. It is clear that reversing the deterioration of the external balance is impossible without fiscal consolidation, something which looks unlikely given the electoral backdrop. At the same time, RON appreciation in real terms driven by persistently high inflation differential looks unsustainable.

Fig 1 Different perspectives to real rates



Source: NIS, NBR, ING

Fig 2 Trade deficit – the widest since 2010



Source: NIS, ING

The NBR governor sounded happy about the headline inflation print today. The details are less rosy, at best. At the same time, he reiterated concerns about the widening C/A deficit. The central bank is again in a position to walk a fine line between rates and FX. It may have some success on inflation, but without fiscal adjustment the external imbalances are set to widen further. A fiscal consolidation is long overdue, but with elections ahead things are apparently going in the opposite direction.