

Romania: no surprises on the inflation front

June inflation came in at 2.6% year-on-year, close to our 2.5% forecast, as prices advanced by a mere 0.08% from the previous month. The future path looks stable around the 2.5% central bank target

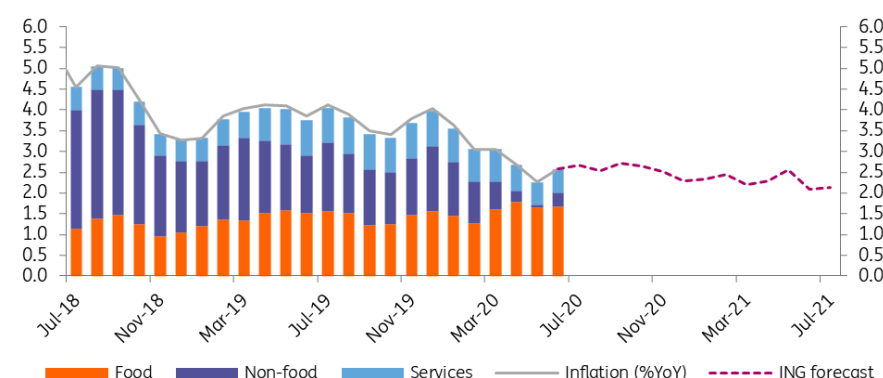


People shopping in a supermarket in Bucharest

Although the 0.08% monthly advance in June was just shy of the 0.05% in May, the underlying drivers have changed somewhat. Food prices contracted by 0.4% over May, the first monthly contraction since Sep-2019, while non-food prices expanded by 0.3%, the first advance in the last five months. The services sector, on the other hand, offered few surprises as price decreases are quite rare here, with the last one happening in February 2017.

Looking forward, better behaved food prices should last at least through the summer which will help headline inflation to stay close to today's print. Another factor which should keep inflation in check will be the already announced 1.9% reduction of electricity prices starting 1 July 2020 and a likely (though gradual and less predictable) fall in natural gas prices following the market liberalisation that took place on 1 July 2020. On the opposing side, fuel prices still have some potential to push inflation higher, together with some limited FX weakness.

Inflation and components



We continue to believe that the central bank will hold on to its current 1.75% key rate level at least through 2020 and 2021. We admit that the room for policy easing looks ample, but – consistent with its previous behaviour – we think that the National Bank of Romania will look through the current cycle and prefer to avoid a situation where it lowers the policy rate in 2020 and has to increase it next year. In the end, even in the unlikely scenario of another 25 basis point cut to 1.50% (not our base case though) we do not think that market rates will proportionately move lower and continue to see the 3-month Robor rate close to 2.00% over 2020 and 2021.

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