Romanian inflation edging higher in February

The annual inflation rate reached 3.2% in February 2021, closely matching the consensus and our view. We revise higher our 2021 average inflation forecast from 2.7% to 3.0% and the year-end from 3.0% to 3.3%

Romanian seasonal workers wait for check-in at the Avram Iancu international airport, in central Romania.

Source: Shutterstock

3.2% February inflation

February inflation printed 3.2%, a touch above our 3.1% estimate, which is due exclusively to a marginal increase in electricity prices versus our expectation of a small decrease. After the sharp monthly spike in electricity prices in January (+18.4%), it seems that consumers are in no hurry to look for alternatives on the competitive market. This has helped core inflation to stay at 4.3% in February -similar to January, and significantly above the latest central bank projections. We expect the core inflation rate to remain firmly higher than headline inflation at least through the second quarter of 2021, followed by a stabilisation in the 3.0-3.5% range for the rest of the year.

While on the upside there are still plenty of factors which can still surprise us, it is relatively difficult to find some corresponding downside influences, except for some negative pandemic-related surprises. Looking forward this year, we already have a rather benign view on both food and non-food prices while on the services side we feel comfortable in anticipating some short-term price pressures, given the prospects for the economy to work at full speed in the second half of the year.

Limited policy reaction

Having all this in mind, we are revising higher our 2021 average inflation forecast from 2.7% to 3.0% and the year-end from 3.0% to 3.3%. Unless pandemic-related developments require harsher restrictive measures (unanticipated at this point), the risk balance still looks mildly tilted to the upside. However, we prefer to be a touch on the conservative side and wait for the economy to confirm the strong recovery, which is widely anticipated now.

Policy-wise, the central bank will likely try to look through this inflation rise and take a middle-way approach in order to balance the inflation prospects with the upward FX pressures and recent bond yields dynamics. We maintain our views for no change in the key rate at least through the first half of 2022, limited FX depreciation (we stick to our 4.92 year-end forecast for the EUR/RON) and careful liquidity management, with liquidity surpluses more likely to be the exception than the norm. Should sell-off episodes occur in the bond market, the central bank will likely try to contain excessive volatility, but large-scale purchases are unlikely in our view.

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