Romanian inflation finally dips into single digits

After a couple of months of questionable inflation data, July confirmed that double-digit inflation prints are now safely behind us. However, consistently strong wage advances might complicate the disinflation story as the 2024 electoral year approaches

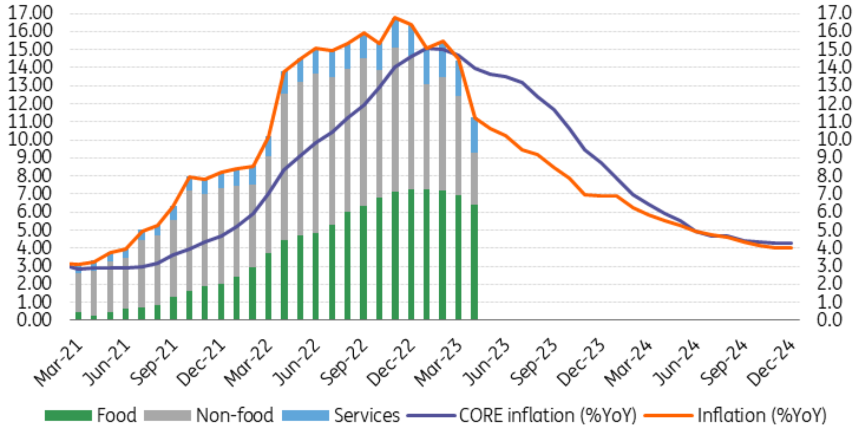
Bucharest, Romania. Food prices decreased in July by 0.5% versus June

The 9.44% July inflation print surprised marginally to the downside (vs our 9.60% estimate) due almost exclusively to lower electricity prices. Recently-adopted caps on the mark-ups of basic food products seem to be working already, slightly ahead of schedule, and might cause another downside surprise to August inflation, which we currently estimate at around 9.0%.

To put a number on it, food prices decreased in July by 0.5% versus June (+16.3% year-on-year), which marks a return to more usual seasonal behaviour. Non-food items advanced by 0.25% (+4.3% YoY) with pretty well-behaved price dynamics across the subcomponents, while services remained a mild outlier, advancing by 1.00% monthly (+11.6% YoY), a slight upset in an otherwise positive inflation print.

Perhaps the less-than-positive news for today comes from core inflation which proves to be quite sticky, falling to 13.2% in July from 13.5% in June. At this moment it is not certain that we will see core inflation below 10% this year, though our base case is that it will dip below in December. In any case, core inflation is probably less of a concern for the National Bank of Romania (NBR) right now, as it most likely wants to see headline inflation safely lower first.

Inflation (YoY%) and components (ppt)



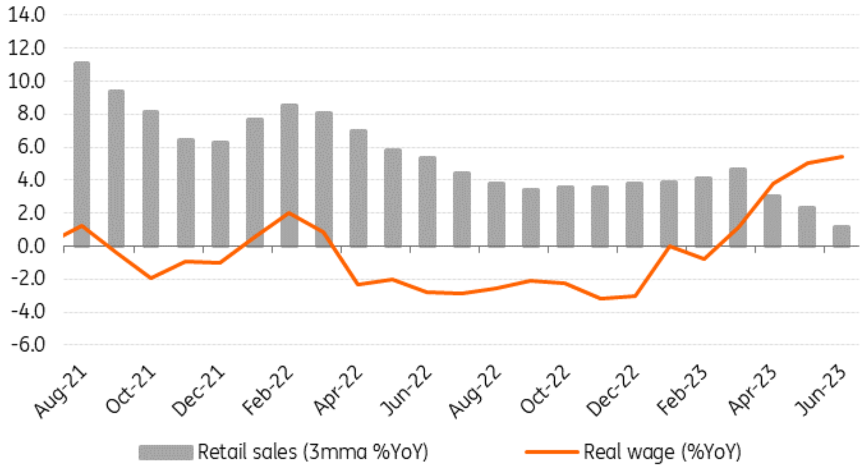
Source: NSI, NBR, ING

Strong wage growth is here to stay

The average net wage advance continues to impress, printing at +15.7% in June and it looks increasingly likely we'll see full-year average wage growth above 15.0% in 2023. Besides the usual sectors which have posted above-average wage advances lately (e.g. agriculture, IT services, transportation etc.), June saw a whopping 28.7% increase in the public education sector's wage, boosting the general public sector average wage growth to 14.0%, not far from the 16.1% growth in the private sector. This trend is most likely to continue in the coming quarters, given recent and ongoing public wage demands and the approaching electoral year.

The extent to which the strong wage advance will filter into inflation is still unclear, given that it overlaps a period of fiscal uncertainties, economic slowdown and still relatively high interest rates which are more stimulative for savers. However, it is also difficult to believe that it will have no effect either. As recently underlined by the NBR's Governor, Mugur Isarescu, wage-led inflation might prove quite dangerous and tricky to control, given that it could require a further restriction of the aggregate demand via even higher interest rates.

Positive real wages to support consumption



Source: NSI, ING

We maintain our estimate of a 6.9% year-end inflation reading, though we admit that risks are mildly to the upside on the back of the recently announced (but not yet adopted) fiscal package. These risks have been clearly underlined by the NBR as well, as they indeed have the potential to derail the disinflation story. On the other hand, next year's profile hasn't changed much, as we see headline inflation below 7.0% (NBR's key rate) in February 2024, followed by a gradual descent toward the 4.0% area by the year-end, where our projection also stabilises for the medium-term.

All in all, we remain reasonably confident that the NBR will start the cutting cycle in the first half of 2024, with a total of 150bp cuts by the year-end. If anything, risks are for the cycle to be more backloaded rather than frontloaded. To the extent that the global risk sentiment will not worsen, it is likely that the accommodative liquidity conditions are here to stay for longer, though we tend to be increasingly cautious about this.

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