

National Bank of Romania preview: waiting for inflation to fall

The National Bank of Romania (NBR) will announce its latest policy rate decision on 10 May. We expect the key rate to stay at 7.00% with no forward guidance. Questions about liquidity surplus and NBR's surprising bond purchase in March might be addressed a few days later during the presentation of the new Inflation Report

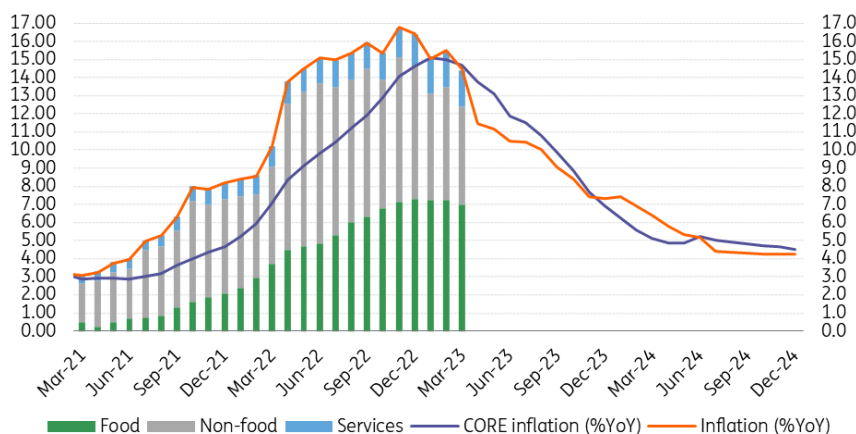


The National Bank of Romania in Bucharest

The context

Last week [we outlined](#) our latest calls for global central bank decisions this month. In the case of NBR, we argued that a clear consolidation of the current disinflationary trend will be needed before the central bank makes its next decision; we're expecting a cut in the first quarter of 2024. Real positive rates (i.e. inflation below the key rate) might be the trigger for action. Our inflation estimates indicate that this could be the case in February-March 2024 when inflation should dip below 7.00%.

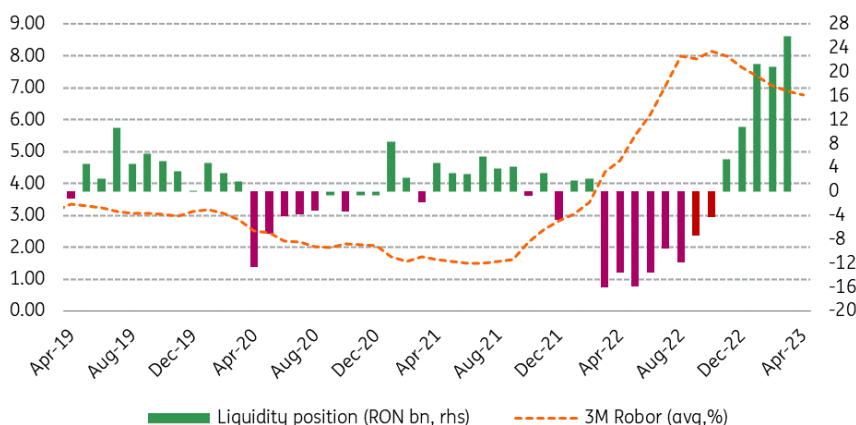
Inflation (YoY%) and components (ppt)



Source: NSI, ING

In practice, however, the NBR seems to have already switched to a much looser policy stance than indicated by the key rate level. The liquidity surplus in the interbank market seems to be higher and more persistent than ever before, pushing market rates well below the key rate and making the 6.00% deposit facility more relevant than the 7.00% key rate. Given no meaningful upside pressures on EUR/RON, the NBR seems to be tolerating this situation as it has not intervened to mop up liquidity via open market operations.

Liquidity surplus at historic highs



Source: NBR, ING

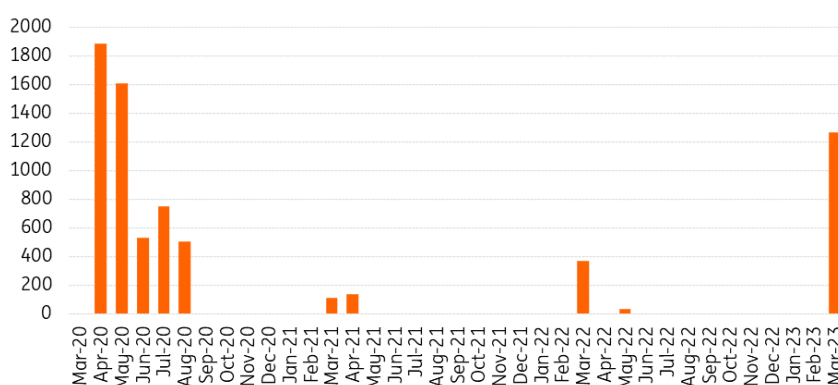
Economic growth in Romania is visibly decelerating, although the still robust wage growth is keeping private consumption afloat, with retail sales actually accelerating by 2.2% in the first quarter of the year versus the previous quarter (5.1% in annual terms). Overall, as outlined by NBR in its last policy meeting, the economic slowdown is likely to be more modest than anticipated by the central bank, implying a slightly above-expectation output gap.

A new Inflation Report to confirm the disinflationary trend

Perhaps more interesting than the monetary policy decision itself will be the presentation of the May Inflation Report which should take place a few days later and incorporate NBR's latest inflation projections. Typically, the forecast revisions increased the short-term outlook while lowering the longer-term, but this time we expect the NBR to broadly maintain its forecasts from the previous report.

An interesting development that might be addressed during the press conference is the fact that NBR purchased bonds from the secondary market in March. In previous years, the NBR justified bond purchases either by the need to provide liquidity to the banking system or by the need to address secondary market dysfunctions. Given there was already a liquidity surplus in March and the secondary bond market was enjoying one of its best months ever, the motivation for the bond purchases must lay elsewhere.

Monthly bond purchases (RON million)



Source: NBR, ING

What to expect

We believe that NBR will stay on course and keep the key rate unchanged both on 10 May and for the remainder of 2023. Should any upside pressures on EUR/RON emerge, the NBR will likely be more than willing to provide euro liquidity to the market in order to mop up some of the local currency surplus.

Speaking of the currency, we have an already long-standing view that EUR/RON will be allowed to shift some 2.0-3.0% higher later this year, most likely when inflation is credibly within single digits. While we maintain our view, we must also notice that upside pressure on the pair has not been material and that the adjustment might take a bit longer to occur.

Externally, geopolitics (and the side effects) aside, we are paying close attention to other regional central banks' behaviour (especially the National Bank of Poland), while internally, the fiscal side of the policy mix shows some signs of weakness as revenues undershot expectations in the first quarter.

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