Serbia: Central bank keeps key rate on hold at 3%

Though inflationary pressures are fairly benign, the National Bank of Serbia opted to wait and see how external developments unfold. We believe there is still room for one more rate cut this year, but the window of opportunity will soon be closing

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We called for a 25bps cut in our NBS preview, based mainly on the benign inflation outlook for the medium term and strength in the Serbian dinar. In the press release which followed today's decision, the NBS acknowledged that inflation "should approach the target mid-point of 3.0% in the second half of 2019" and that inflation expectations are well contained.

With this in mind, we find little reason on the domestic side for keeping rates on hold, besides the need to further assess the impact of previous rate cuts. Hence, we believe that the main reason for today's decision stems from the external environment. On this topic, the NBS noted the uncertainties surrounding oil prices and diverging policies of the Federal Reserve and European Central Bank- both of which seem fairy contained.

We believe that the window of opportunity for policy easing is getting narrower, as inflation has probably bottomed in April and should follow a slower upward trend going forward. An eventual rate cut at the next couple meeting could be on the table if the currency strengthens significantly, as the inflation outlook alone doesn't seem to be convincing enough for the NBS. A rate cut is likely to be accompanied by a further narrowing of the standing facilities corridor to ±1ppt from ±1.25ppt to partially offset its impact.

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