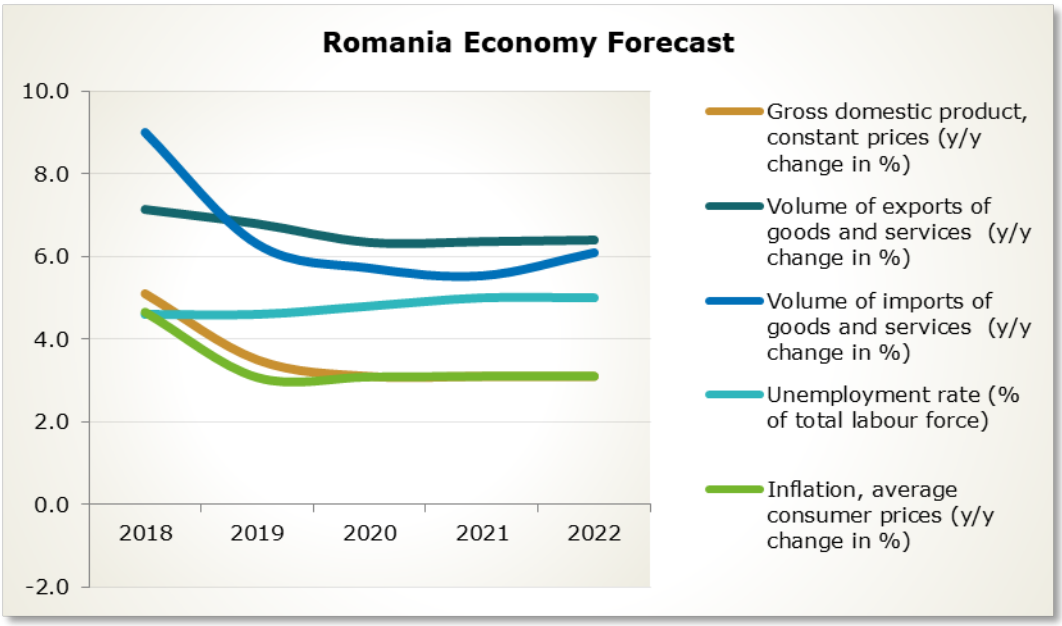
ROMANIA ECONOMY REPORT

2017

CONTENTS

1. MACROECONOMIC SNAPSHOT AND FORECAST

ROMANIA – MACROCECONOMIC SNAPSHOT AS OF END-2017	
GDP Growth	*7% y/y*
Industrial output	*8.2% y/y*
Industrial sales	*11.7% y/y*
Wholesale	*7.5% y/y*
Retail	*10.9% y/y*
Average annual inflation	*1.34%*
Unemployment rate	*4.93%*
Number of building permits	*18.8% y/y*
Money supply growth	*11,6% y/y*
Household loans	*7.8% y/y*
BET blue-chip index	*13% y/y*
Gross external debt	*EUR 93.477 bln*
Current account deficit	*EUR 1.408 bln*
Net FDI inflow	*EUR 4.586 bln*
Foreign trade deficit	*EUR 11.912 bln*
Number of foreign tourist overnights	*-11.7% y/y*

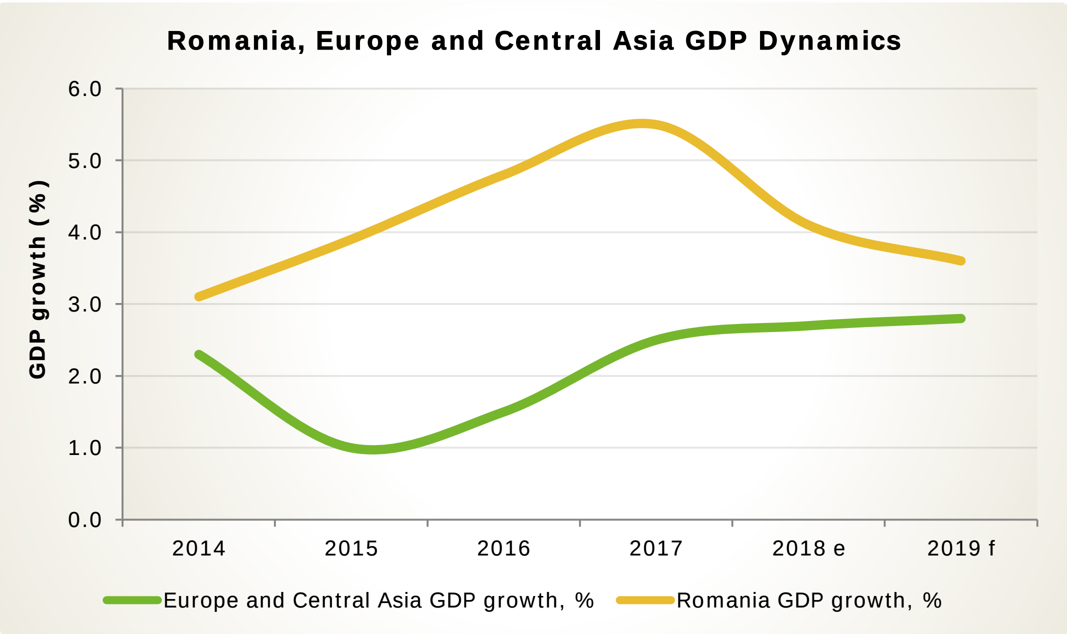


Source: International Monetary Fund (IMF) World Economic Outlook Database - April 2018

In 2018, the economic growth in Romania is expected to decelerate from the high level in 2017, according to IMF forecasts. Main factors for expected GDP slowdown include a waning fiscal impulse, low public investment, slow progress on structural reforms, and tightening financial conditions. IMF projects a growth of about 5% in 2018 and to slow down towards 3% over the medium term.

Risks to the outlook are tilted mostly to the downside, according to IMF. Global financial volatility, further deterioration in fiscal and external balances, or weakening of institutions could dent investor confidence in Romania. The continuation of current expansionary policies would undermine the country's capacity to withstand a severe shock, IMF warns.

According to the fund, a prudent mix of fiscal consolidation and monetary tightening would avert overheating, while reducing the fiscal and external deficits, and enhancing macro-financial stability. Monetary policy needs further tightening to rein in inflation and anchor expectations, given the pressure from global energy prices, strong domestic demand, a tight labour market, and recent currency dynamics. A more conservative fiscal stance would reduce the burden on monetary policy and help improve the balance between consumption and investment. If this task is left to monetary policy alone, interest rates would have to be raised to such a level that will increasingly weigh on investment and competitiveness, IMF concludes.



Source: World Bank, Europe and Central Asia Economic Update, April 2018

According to the latest World Bank forecast, the Romanian GDP will likely expand by 5.5% in real terms in 2017 on strong consumption growth, which will be supported by VAT rate cut and minimum wage increase. In the same time, consumption growth will contribute to the widening of the current account deficit to 3.1% in 2017, from 2.4% a year earlier.

Positive output gap and increased import prices will drive inflation upwards while fiscal relaxation policies are likely to put pressure on the consolidated budget deficit, according to the World Bank forecasts. In 2017, inflation will return with general price increase of 2.0% in 2017 and 2.5% in 2018 from deflation of 1.5% in 2016.

In 2019 and 2020, the bank forecasts economic growth of 4.1% and 3.6%, respectively. Risks to the forecast include adverse exogenous shocks, which would negatively affect the economic growth as the government is already pursuing pro-cyclical fiscal policy, which limits the space for manoeuvre.

Romania – GDP, Inflation, Current Account Balance and FDI Dynamics (y/y change in %)

	2014	2015	2016 e	2017 f	2018 f	2019 f
Real GDP growth, at constant market prices, y/y cha	3.1	3.9	4.8	5.5	4.1	3.6
Private Consumption	4.4	5.5	7.3	8.0	6.5	6.4
Government Consumption	0.5	-0.7	3.3	2.8	4.3	3.1
Gross Fixed Capital Investment	3.2	8.3	-3.3	1.1	4.5	4.2
Exports, Goods and Services	8.0	5.4	8.3	9.6	7.4	6.3
Imports, Goods and Services	8.7	9.2	9.8	10.1	8.3	7.7
Real GDP growth, at constant factor prices (by sectors)						
Agriculture	4.3	-11.8	0.0	6.0	2.1	2.1
Industry	3.2	6.6	1.7	5.9	2.7	1.6
Services	3.1	4.7	7.3	5.2	5.1	4.8
Inflation (Consumer Price Index)	1.1	-0.6	-1.5	2.0	2.5	2.8
Current Account Balance (% of GDP)	-0.5	-1.2	-2.4	-3.1	-3.5	-3.8
Net Foreign Direct Investment (% of GDP)	1.6	2.2	2.4	2.5	2.8	2.8

Source: World Bank, Europe and Central Asia Economic Update, October 2017

2. REAL SECTOR

2.1. GROSS DOMESTIC PRODUCT (GDP)

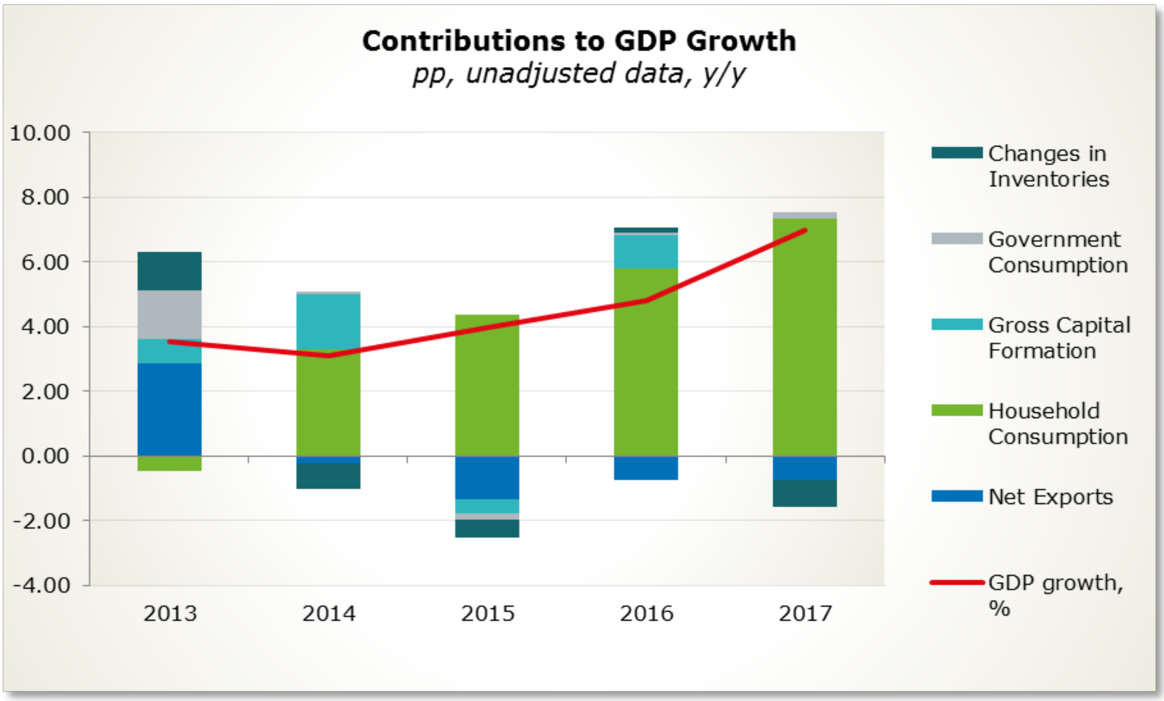
GDP growth accelerated to 7% y/y in 2017, one of the fastest among EU-28 countries

The country's GDP increased by a real 7% y/y and totalled RON 157,668 bln in 2017, according to the data from the National Institute of Statistics (INSSE). This is up compared to an annualized growth of 4.8% in 2016.

Household consumption was the main driving engine of the Romanian economy in 2017. Surging by 9.2% y/y in real terms in 2017, the household consumption contributed by 7.33 pp to the overall GDP expansion. Consumer demand was strongly boosted by pro-cyclical fiscal measures designed to increase household income. The government made a series of VAT reductions and minimum wage increases in recent years. The most solid VAT rate drop was in June 2015 from 24% to 9.0% for food products. It was followed by VAT decrease from 24% to 20% for all other products in January 2016. The government decided to support the lower income Romanians by increasing the minimum monthly gross wage by 19% to RON 1,250 in May 2016 and by extra16% to RON 1,450 (EUR 322) in February 2017.

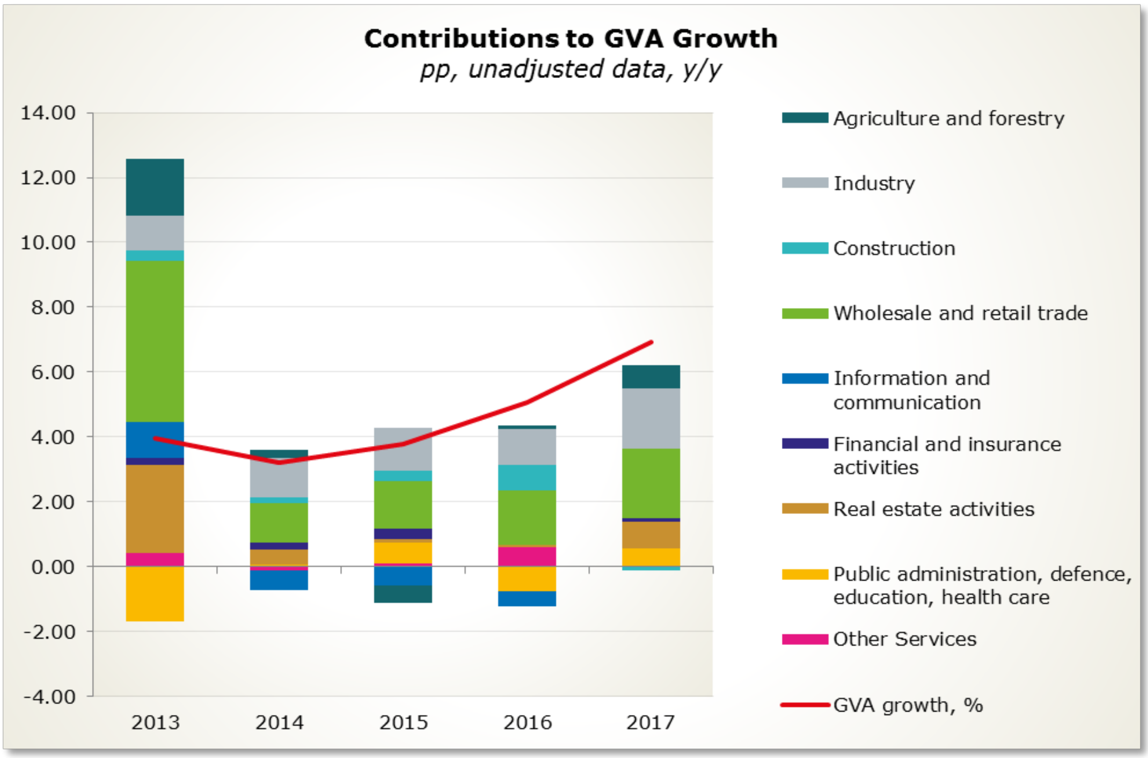
Gross capital formation also marked a sharp rise in its contribution to the growth of the national economy in 2017. It increased by 4.5% y/y in 2017 and contributed to 1.04 pp to the GDP increase in 2017. According to the NBR, the positive evolution of private investment (due to the cyclical advance in residential construction and the slight step-up in equipment purchases) was offset to a large extent by the decline in public investment. Imports continued to cover a significant part of domestic absorption, thus eroding the favourable influence coming from the upward trajectory of exports, supported by foreign direct investment and stronger demand from European economies. Exports of goods and services grew up by 9.1% y/y to RON 107.111 bln in 2017 while imports increased faster, by 10.7% y/y to RON 163.486 bln.

The slow progress of structural reforms and reforms for boosting EU funds absorption is likely to weigh on the country's capital investments.

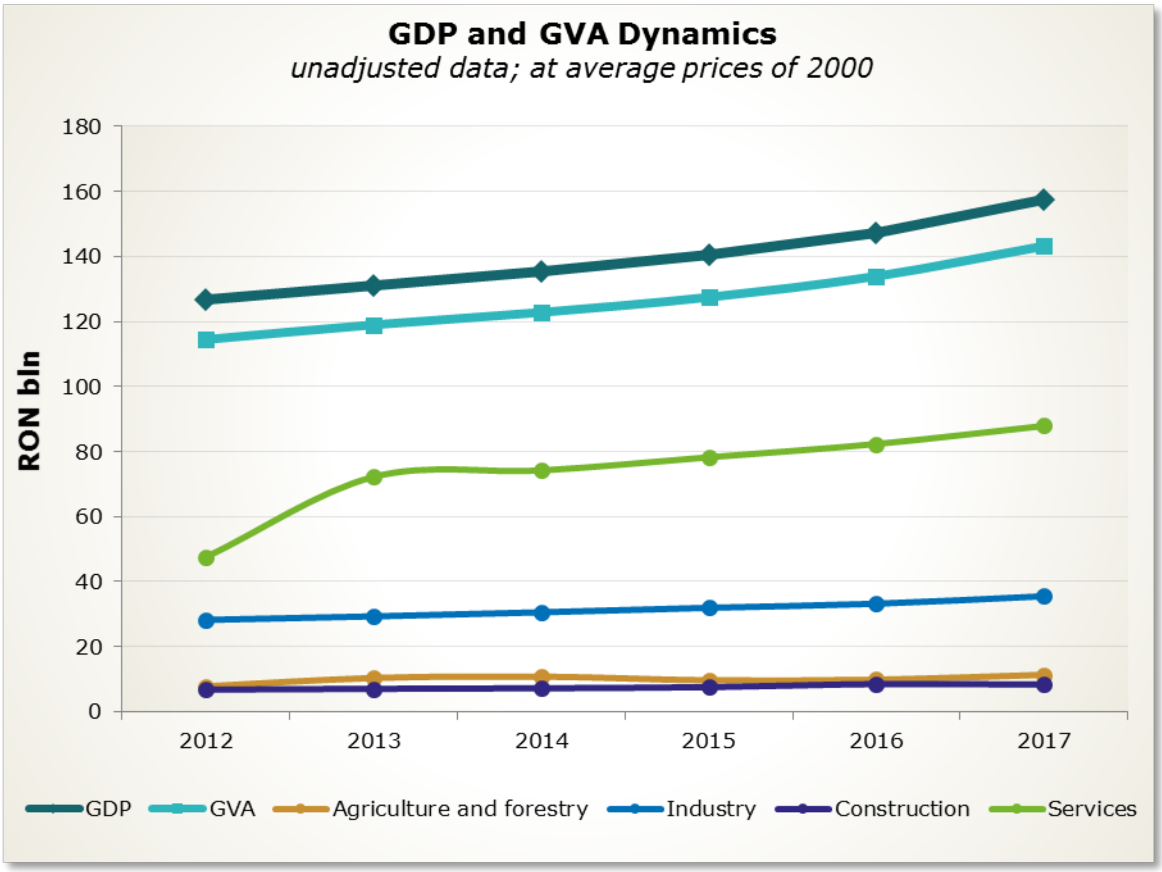


Source: INSSE; SeeNews calculations
Note: Non-additive data due to direct chain-linking of GDP and its components. Contribution of changes in inventories has been derived as a residual.

The gross value added (GVA) generated by the national economy increased by 6.9% y/y in 2017 and totalled RON 143.225 bln. The industrial sector expanded by 7.0% y/y while the services sector recorded a 6.8% annual increase. The agricultural sector registered an annual rise of 15.3% while construction went down by 1.5%. The retail and wholesale trade sector contributed with 2.15 pp to the GVA growth in 2017 on the simulative government policy, which supported consumption. The industrial sector contributed with 1.88 pp to the GVA growth.



Source: INSSE; SeeNews Calculations
Note: Non-additive data due to direct chain-linking of GDP and its components.

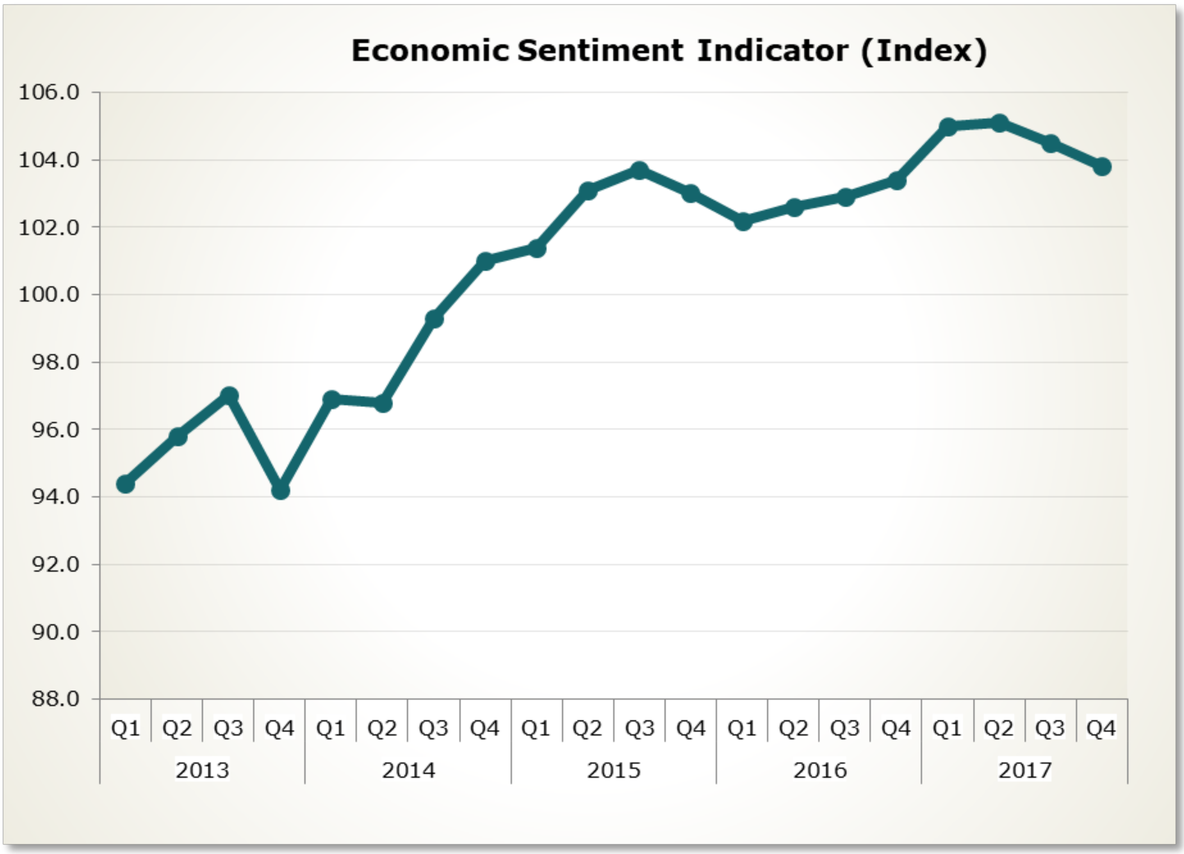


Source: INSSE

2.2. BUSINESS CLIMATE

Economic Sentiment Indicator deteriorated towards the end of 2017

After hitting a record high level of 105.1 in Q2 2017, the economic sentiment indicator set back during the rest of the year, decreasing by 1.2% to 103.8 as of end-2017. The faltering sentiment in H2 2017, reflects the worsening current and expected business conditions over the next 12 months. The worsening economic sentiment implies that over the short term, the outlook for the industrial sector is less bright.



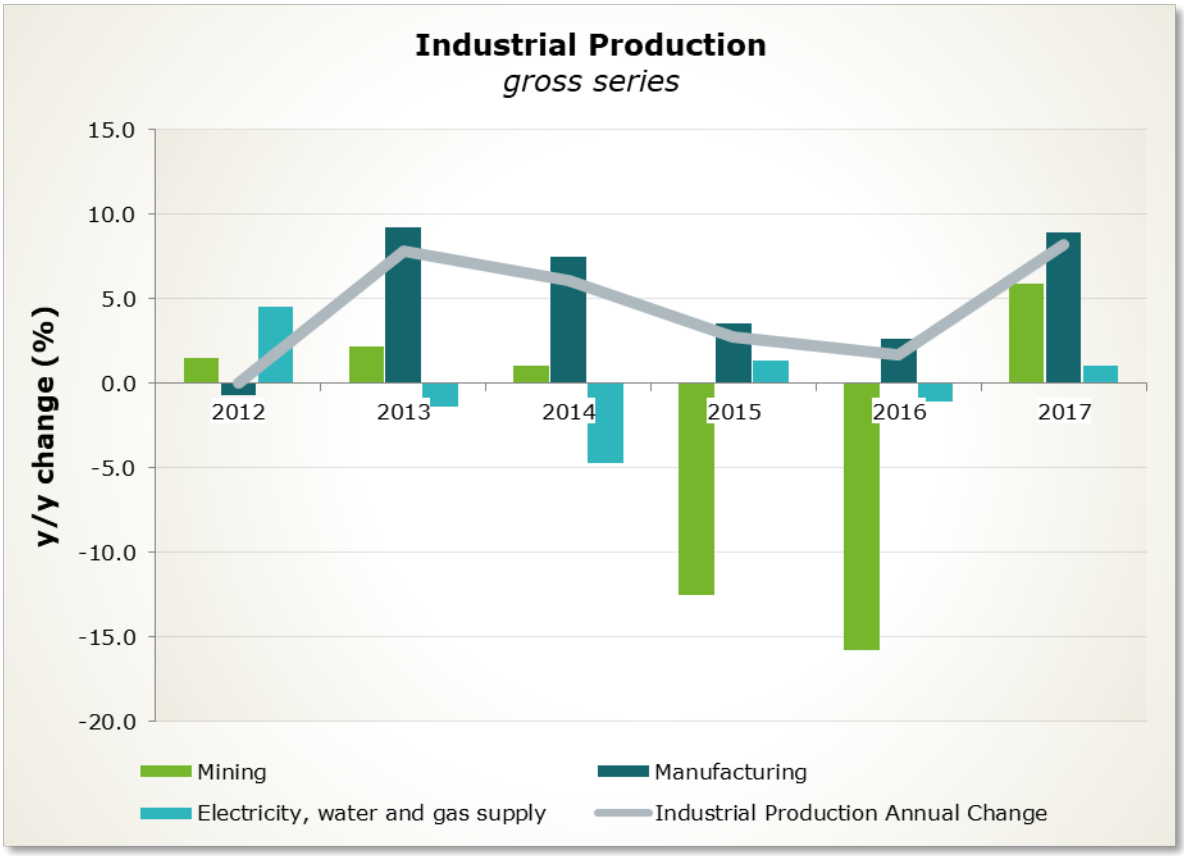
Source: Economic and Financial Affairs, European Commission

2.3. INDUSTRIAL OUTPUT

Industrial production surged in 2017 on strong manufacturing growth

In 2017, industrial output accelerated its pace of growth to 8.2%, up from 1.7% in 2016, according to INSSE. The main driver was the manufacturing industry which expanded by 8.9%, followed by the mining sector with a 5.9% annual increase, while the electricity, water and gas supply sector grew slower, by 1.0% y/y. Manufacture of non-specialised machinery and equipment, electrical equipment and mining support service activities were the sectors with the fastest y/y growth in 2017.

According to NBR, the fastening manufacturing growth was driven primarily by export-oriented sub-sectors such as machinery and equipment, other transport equipment and automotive industry. The latter was fuelled by the successful new models that even helped a carmaker hit a record high in terms of output. A notable annual performance also posted the food industry, thanks to bumper crops and investment in expanding productive capacities, and hydrocarbon processing, as a result of one of the major players expanding abroad and a lower base effect.



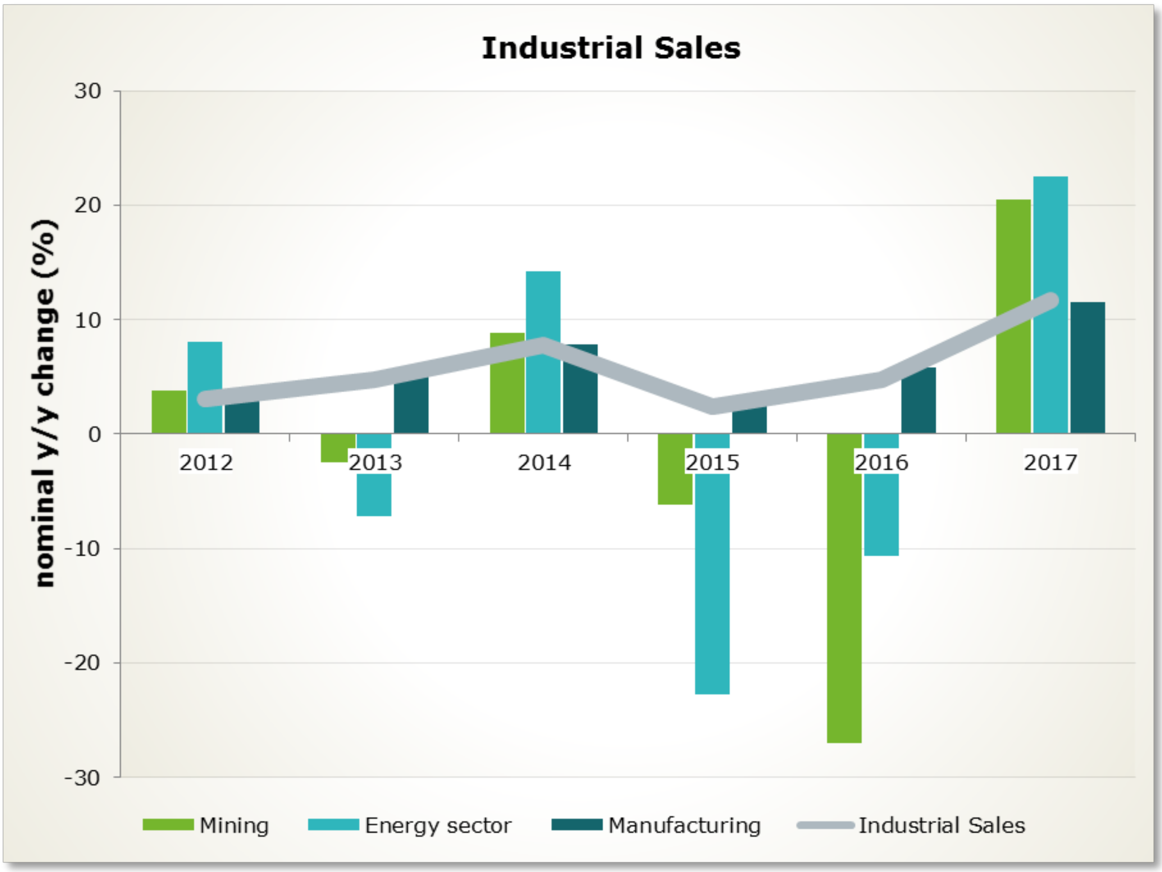
Source: INSSE

2.4. INDUSTRIAL SALES

Industrial sales went up by 11.7% y/y in 2017, as growth was widespread

Industrial sales increased by 11.7% y/y in nominal terms in 2017, according to INSSE data. Sales in the manufacturing industry grew by 10.8% on the year, while the energy sector jumped 11.5% y/y. Mining sales also went up, by 20.5% y/y. The higher rises of the energy and mining sales reflect the lifted commodity prices on the international markets.

Sales of capital goods went up by 16.2%, intermediate goods added 10.2% y/y, durable goods sales increased 5.5% and non-durable goods grew by 5.5% in 2017.



Source: INSSE

2.5. WHOLESALE/RETAIL

Wholesale and retail trade slowed in 2017

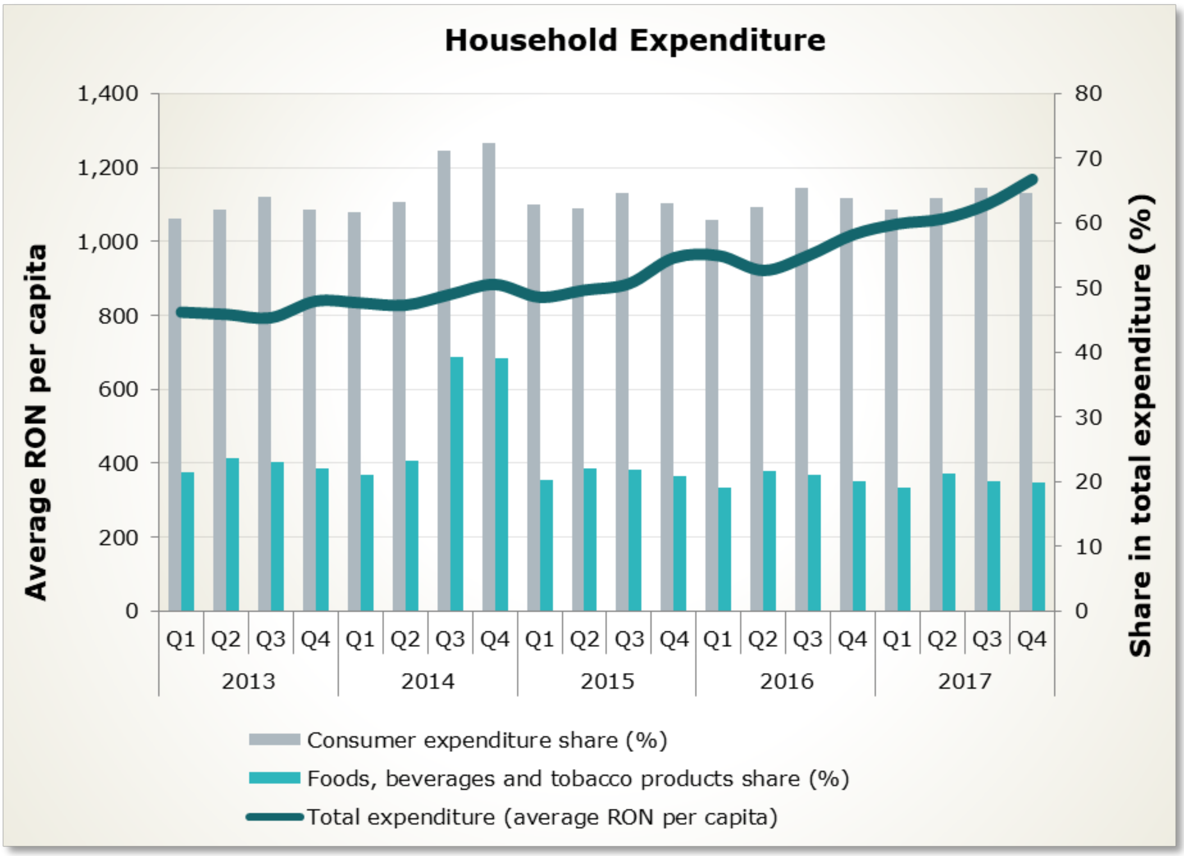
The growth rates of both retail and wholesale trade slowed in 2017 as the stimulus from the wage increase VAT reduction towards the end of 2017 faded. Still, sectors' growth remains solid as there were additional fiscal stimuli in early 2017. Retail sales went up by 10.9% y/y while wholesales trade increased by 7.5% y/y in 2017 compared to growth rates of 13.7% and 7.7%, respectively, during the corresponding period of 2016, according to INSSE data.

According to NBR, the major contribution to retail sales in 2017 was made by purchases of durables, up at a faster annual clip, due to the demand for motor vehicles and furnishings (also via online sales, which displayed a sharply upward slope). Sales of non-durables posted a slower rate of increase, which could be ascribed to a certain flattening trend in demand for food items as the effect from the 7.8% climb in motor fuel sales in January 2017 faded away, after the special excise duty was scrapped.

Source: INSSE

Retail sales of food, beverages and tobacco increased by 6.8% y/y in 2017, retail sales of non-food products went up by 13.2% y/y while the turnover in volume terms of automotive fuel in specialised stores added 12.4% compared to 2016.

Among the wholesale segments, non-specialised wholesale occupied the top position in terms of annual growth with 16.5%, while wholesale of information and communication equipment led the negative ranking with an annual decline of 1.4%.



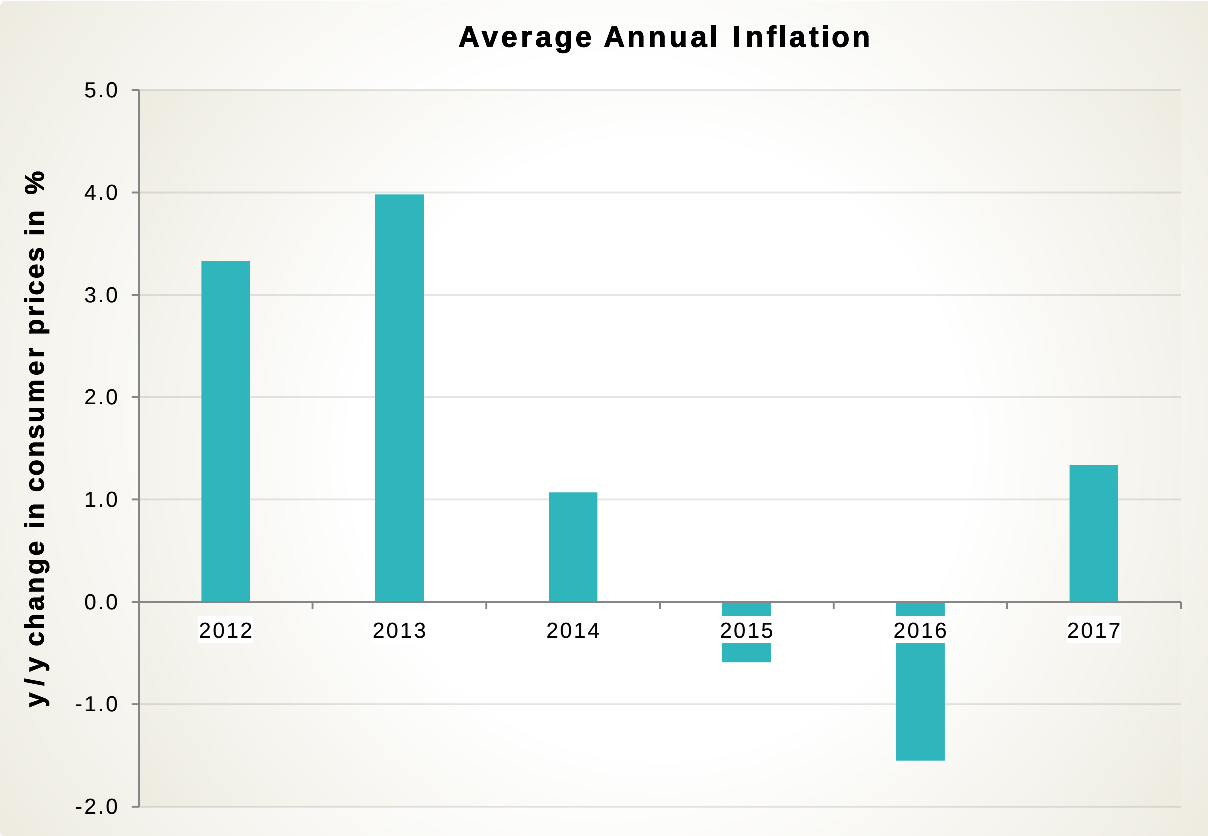
Source: INSSE

2.6. INFLATION

Inflation returned in 2017 on the oil and gas price recovery

In 2017, the average consumer prices in Romania rose for the first time in two years as the country registered an annual inflation of 1.3%, in 2017, INSSE data showed. The main driving force behind inflation in 2017 was the rise of the energy commodity prices on the international markets, namely the oil and natural gas. There were also cost pressures from utilities and labour force, adding to the influence of excess aggregate demand.

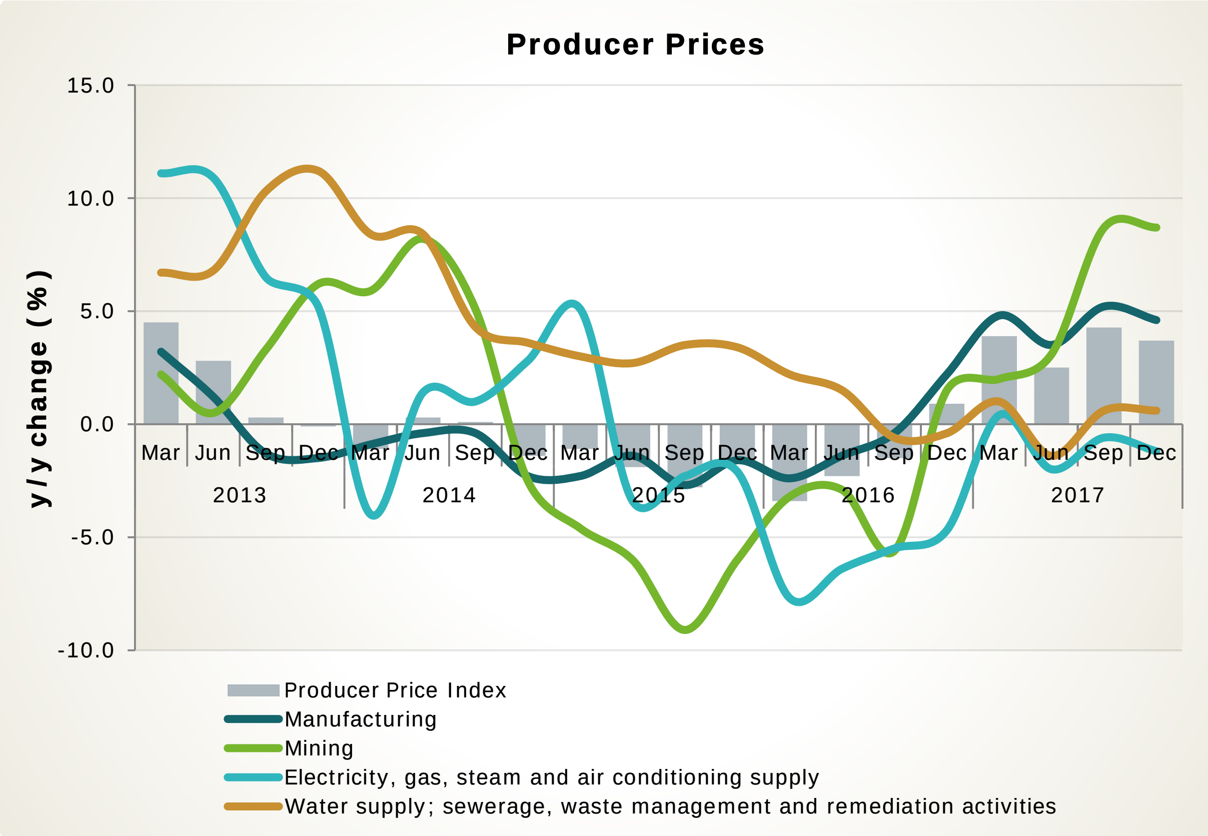
The average price of food and related goods went up by 4.1% y/y in 2017. In the same time, non-food goods were by 4.1% more expensive than a year ago, while the average consumer price of the services went down by 0.2% y/y.



Source: INSSE

The significant hikes in the international prices for metals and energy throughout 2017, gradually passed through to producer prices for intermediate and capital goods, whose annual dynamics followed an upward path.

In 2017, the producer price index grew by 3.7% y/y, driven to a larger extend by producer inflation pressure on the foreign markets - up 5.1% y/y. Producer prices on the domestic market increased by 3.0% y/y. Looking at the main industrial groups, the total price index in the intermediate goods sector jumped the most, by 6.0% y/y, while the energy industry reported the slowest growth rate of 1.7% y/y.



Source: INSSE

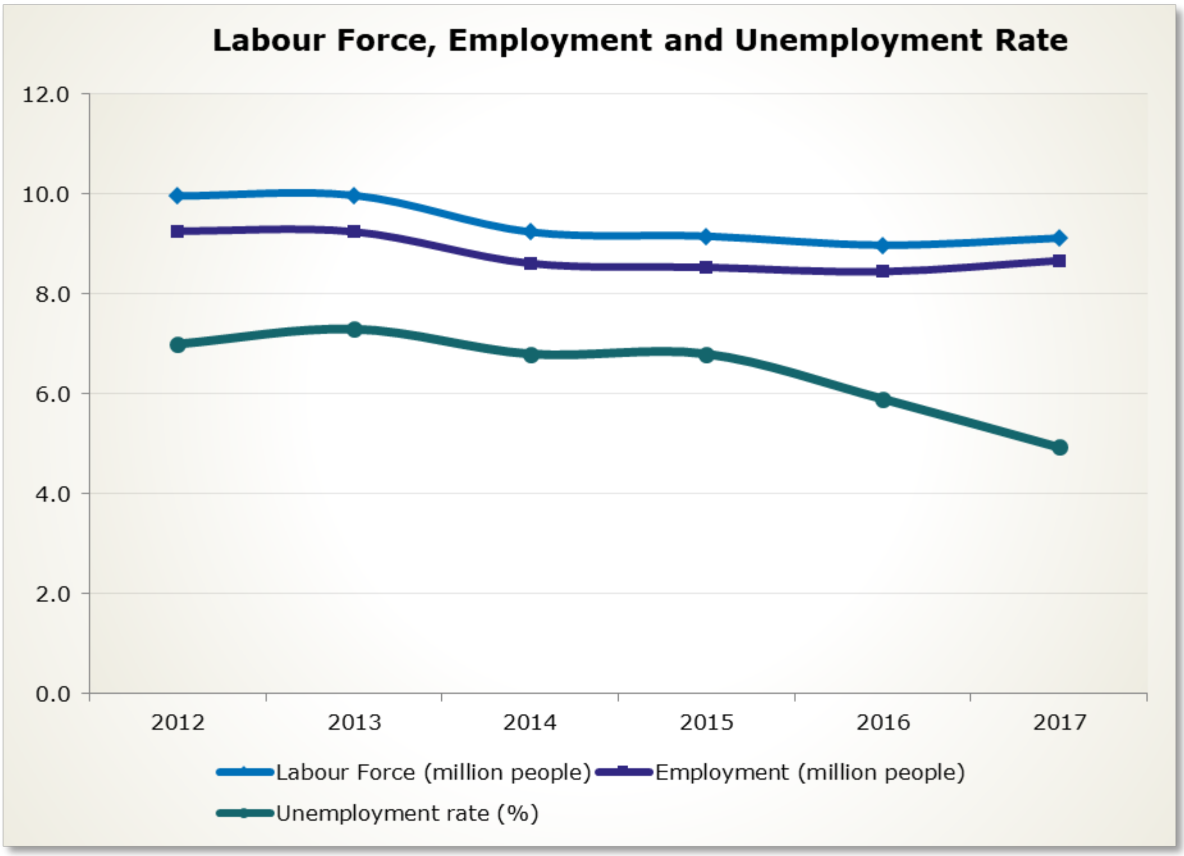
3. LABOUR MARKET

Unemployment rate narrowed y/y to 4.9%y/y in 2017

The downward trend of unemployment rate that has started since 2013, continued in 2017. The dynamic growth of GDP in Romania further reduced the unemployment rate in the country in 2017 to 4.9% from 5.9% in 2016, according to data of INSSE. In this context, labour market conditions remain tight, with employers pointing further to difficulties in hiring skilled workforce, according to DG ECFIN survey.

The employed population aged 15 years and older was 8.670 million, up by 2.6% y/y. The youth (population aged 15-24) unemployment rate improved by 4.9 pp y/y, but still remained high at 18.5% in 2017.

The tightening labour market contributed to the increase of net earnings in 2017, when the average monthly net nominal wage came in at RON 2,384, an annual rise of 14.2%.



Source: INSSE

The highest values of the average net nominal earnings was recorded in computer programming, consultancy, and information service activities, of RON 5,981, while the lowest salaries were recorded in accommodation and food service activities - RON 1,388.

4. CONSTRUCTION AND REAL ESTATE

Number of building permits went up by 18.8% y/y in 2017

The number of building permits issued in Romania in 2017 went up by 18.8% y/y, totalling 48,358, according to INSSE data. The growth was fuelled by the 34.0% y/y rise of permits for administrative buildings to 204, while permits for housing projects grew slower, by 15.8% to 45,564.

The total developed built-up area covered by the residential projects permits also increased by 17.9% to 9.760 million sq m. The total developed built-up area of the permits for administrative buildings soared by 81.3% y/y in 2017.

5. MONETARY POLICY, MONEY SUPPLY, AND BANKING SYSTEM

5.1. RON EXCHANGE RATE

The average exchange rate of the RON against the EUR increased to RON 4.5681 in 2017 from RON 4.4908 a year earlier, according to National Bank of Romania (NBR).

RON Average Exchange Rate			
Foreign Currency	**2017**	**2016**	**2015**
EUR	4.5681	4.4908	4.4450
USD	4.0525	4.0592	4.0057
GBP	5.2143	5.4982	6.1241
CHF	4.1139	4.1195	4.1684

5.2. MONETARY POLICY

The national bank kept the policy rate unchanged at 1.75%

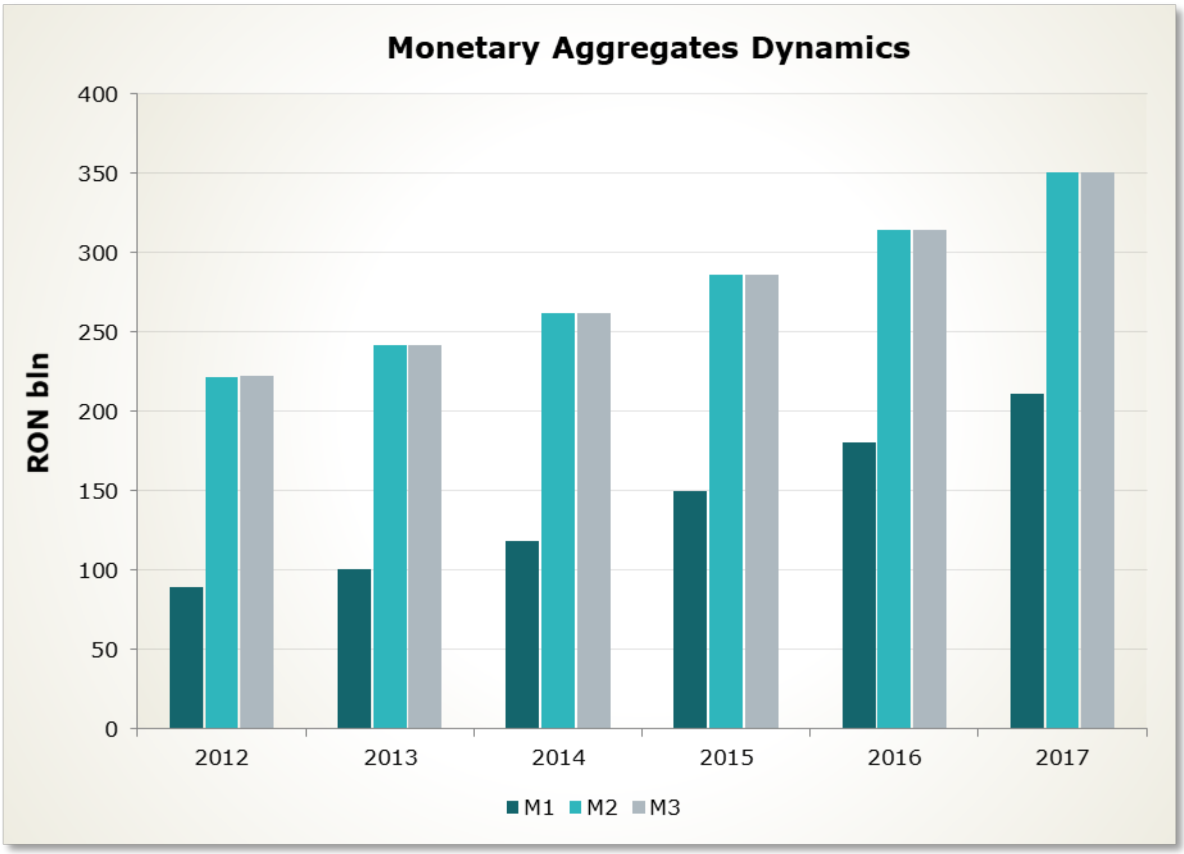
In November 2017, the National Bank of Romania (NBR) decided to narrow the corridor of interest rates on the NBR's standing facilities around the policy rate by another ±0.25 percentage points to the standard width of ±1.00 percentage points, to ensure firm liquidity management in the banking system, to keep unchanged the monetary policy rate at 1.75% per annum, as well as to maintain the existing levels of minimum reserve requirement ratios on both RON- and foreign currency-denominated liabilities of credit institutions.

5.3. MONETARY AGGREGATES

Money supply growth accelerated in 2017

Broad money (money aggregate M3) increased by 11.6% y/y and reached RON 350.6 bln as of end-2017, according to data provided by NBR.

The M2 money supply also grew by 11.6% y/y, to RON 350.5 bln. Money aggregate M1, or narrow money, jumped by 17.1% y/y, to RON 210.7 bln.



Source: NBR

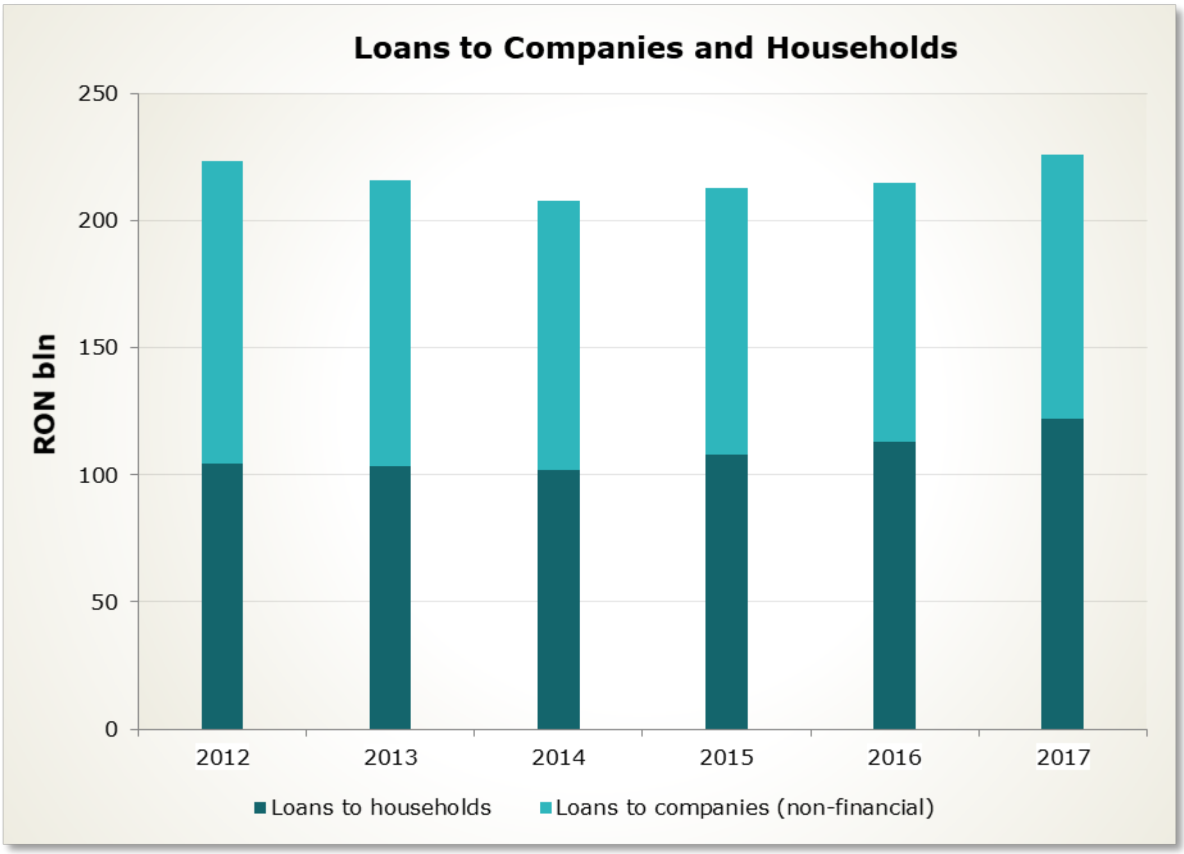
5.4. BANKING AND INSURANCE

Household loans went up by 7.8% y/y in 2017 on strong house purchase credits

Loans to the non-government sector totalled RON 226.0 bln in 2017, up by 5.1% y/y, according to NBR data.

The bulk of the credit growth revival was a result of house purchasing loans by households which increased by 13.2% to RON 66.2 bln. Consumer loans went up by the modest 3.1% to RON 53.8 bln, while loans to non-financial corporations rose by 2.5% y/y to RON 104.2 bln.

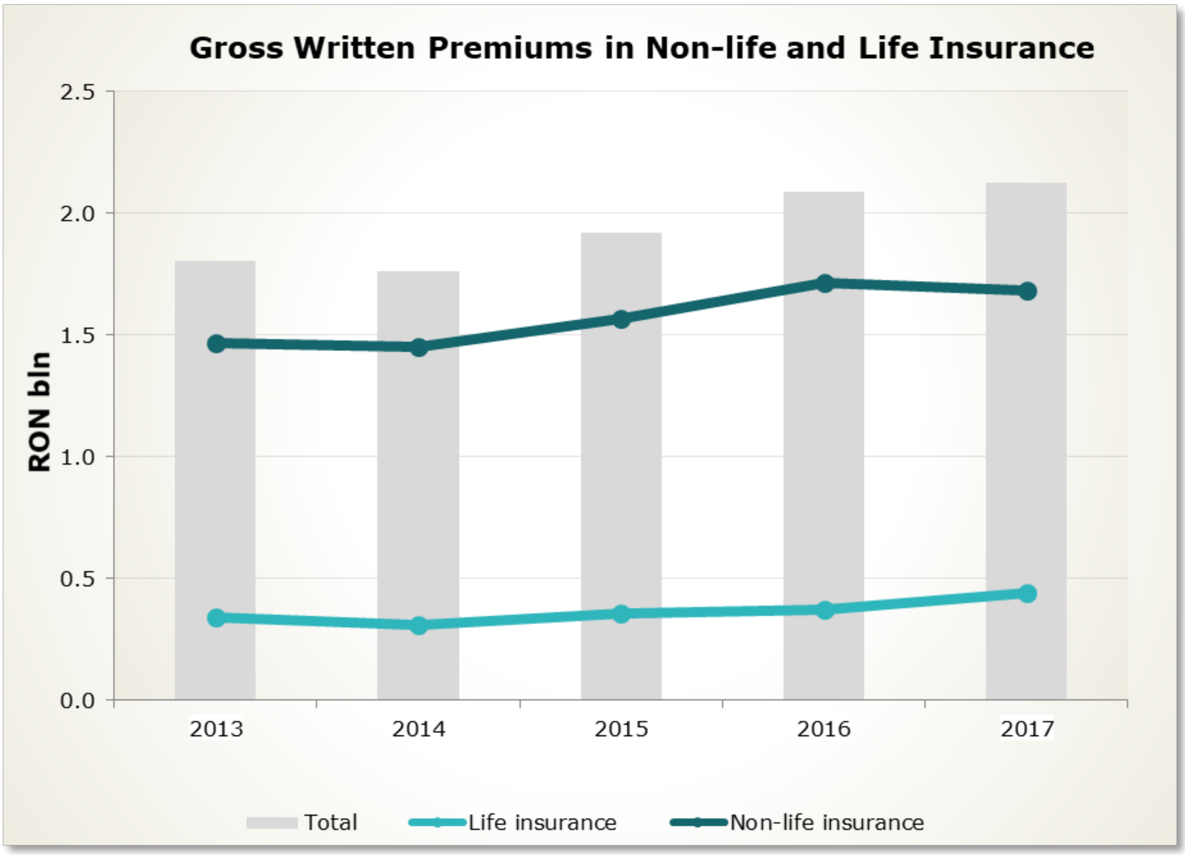
According to NBR survey, in the final quarter of 2017, credit institutions preserved their credit standards on loans for house and land purchase to households and tightened marginally those for consumer credit. As for non-financial corporations, lending conditions applicable to them stayed flat against the previous quarter.



Source: NBR

Insurance premium income up 1.7% y/y in 2017

The total gross written premiums (GWP) of the non-life and life insurance companies were RON 2.125 bln in 2017, up 1.7% y/y, according to the Financial Supervisory Authority (ASF). The growth was driven entirely by the life-insurance sector, which soared by 18.8% y/y to RON 0.442 bln, while the non-life segment decreased by 2.0% y/y to RON 1.683 bln.



Source: ASF

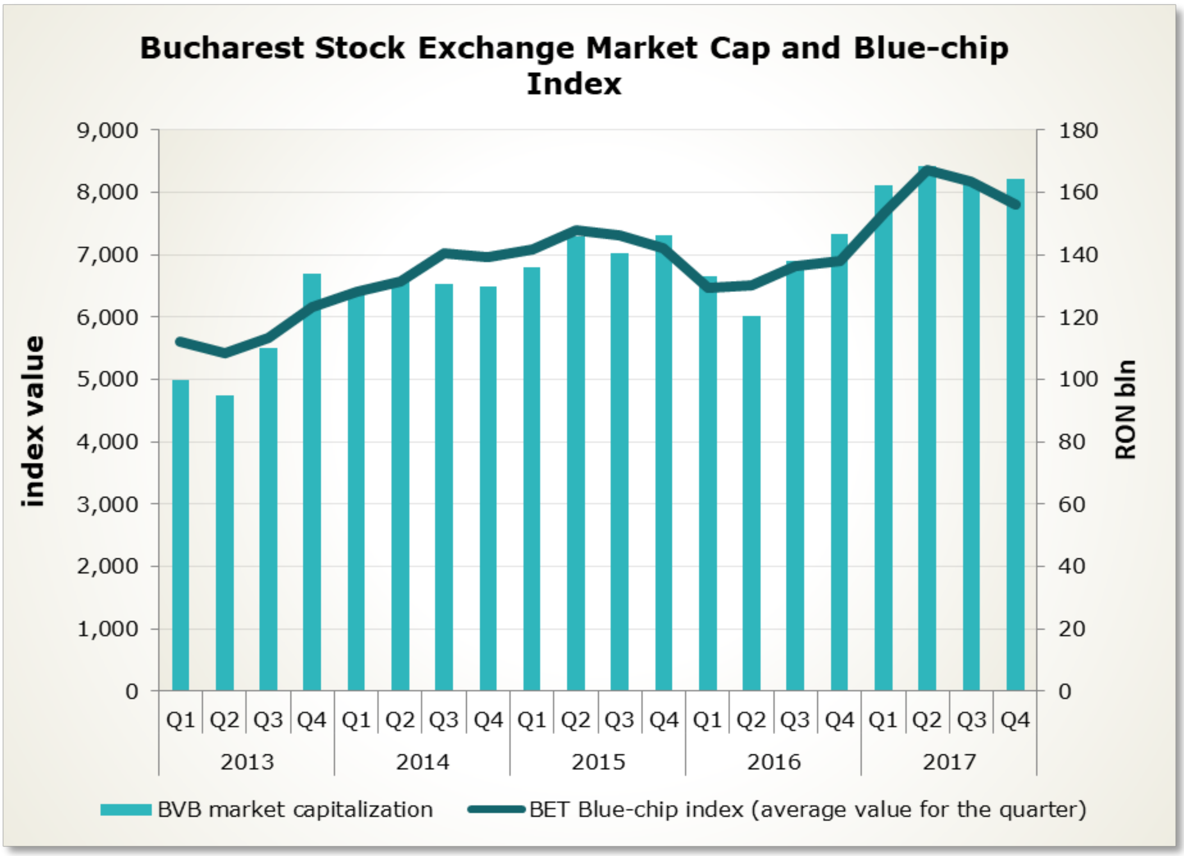
6. CAPITAL MARKETS

Blue-chip BET increased by 13% y/y in 2017

The average value of BET, the blue-chip index of the Bucharest Stock Exchange (BVB), increased by 13% y/y to 7,811.92 points in 2017.

BVB's total market capitalisation came in at RON 164.4 bln as of end-December 2017, up by 1.0% annually.

The total turnover on BVB went up to RON 13.741 bln in 2017, from RON 11.032 bln in the previous year.



Source: BVB

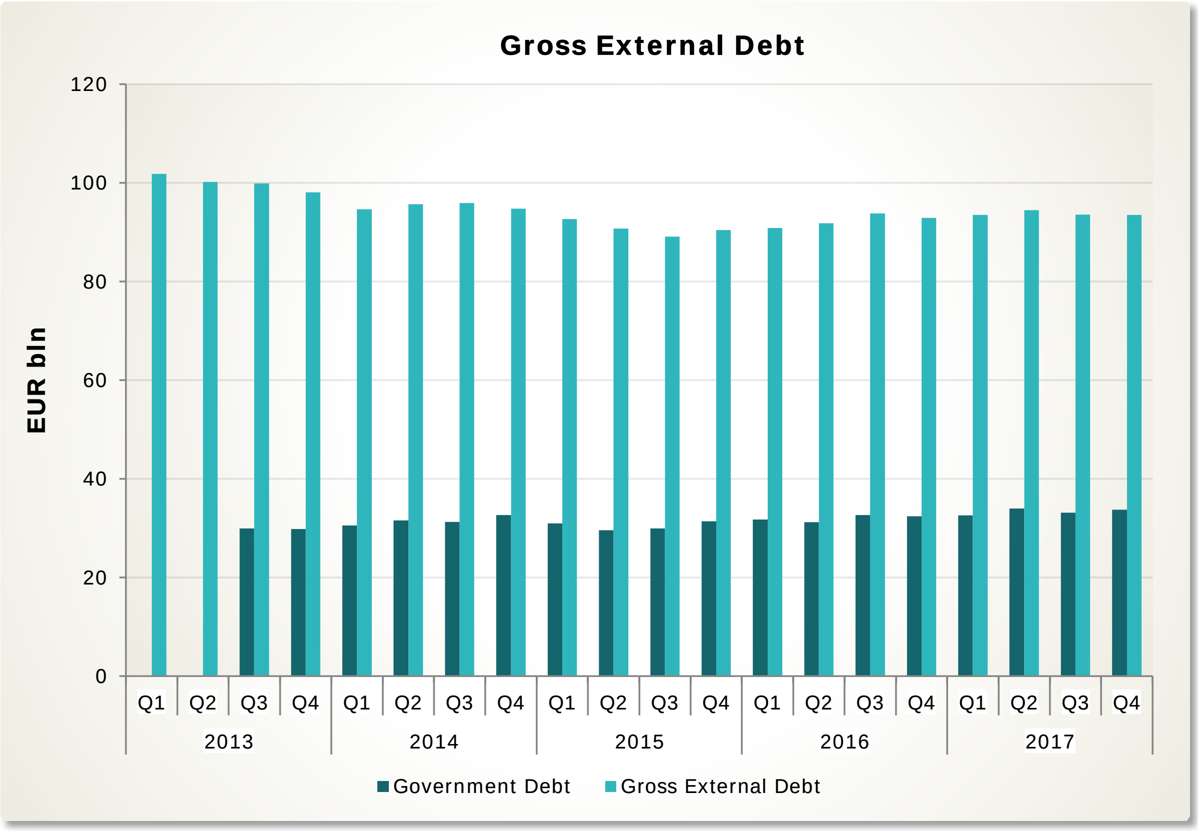
7. EXTERNAL SECTOR

7.1. FOREIGN DEBT

The gross external debt inched up by 0.6% y/y to EUR 93.744 bln as of end-2017

Romania's gross external debt amounted to EUR 93.744 bln in 2017, increasing by 0.6% compared to a year earlier when it amounted to EUR 92.91 bln, according to NBR.

The long-term liabilities amounted to EUR 54.4 bln, or 58.2% of the total debt, and short-term liabilities totalled EUR 12.3 bln, equal to 13.2% of the total debt. The government debt expanded by 4.0% y/y to EUR 33.7 bln.



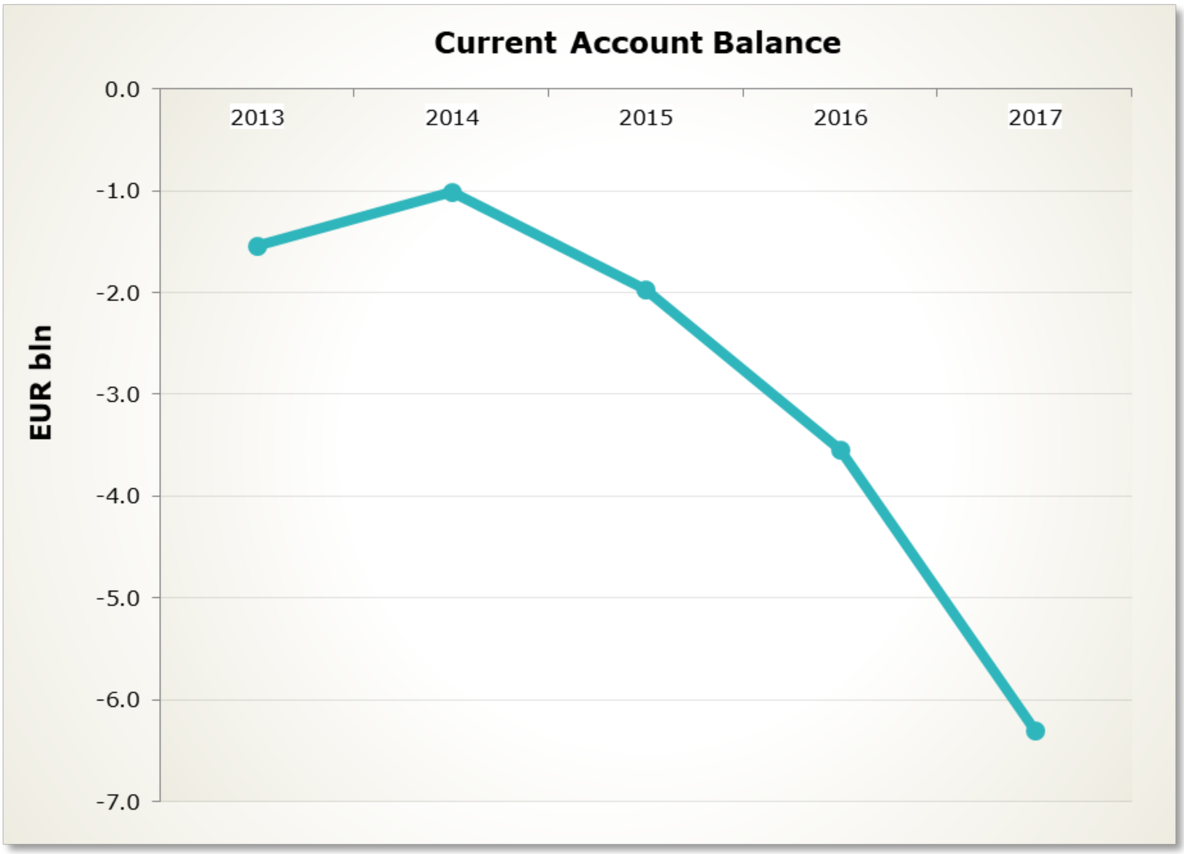
Source: NBR
Editor's note: No data is available for Government Debt for Q1 and Q2 2013

7.2. BALANCE OF PAYMENTS

The current account balance deteriorated further in 2017

Since 2014, there is a tendency of widening of the current account balance, which persisted in 2017. During last year the current account deficit swelled to EUR 6.3 bln, up 77% from EUR 3.5 bln in 2016, according to central bank statistics data. The worsening current account deficit on an annual basis was mainly a result of increased trade deficit with goods, from EUR 9.3 bln in 2016 to EUR 11.9 bln in 2017.

The widening current account deficit was a direct consequence of the rising consumption and the wider fiscal deficit which have increased domestic demand that domestic production could not immediately meet.

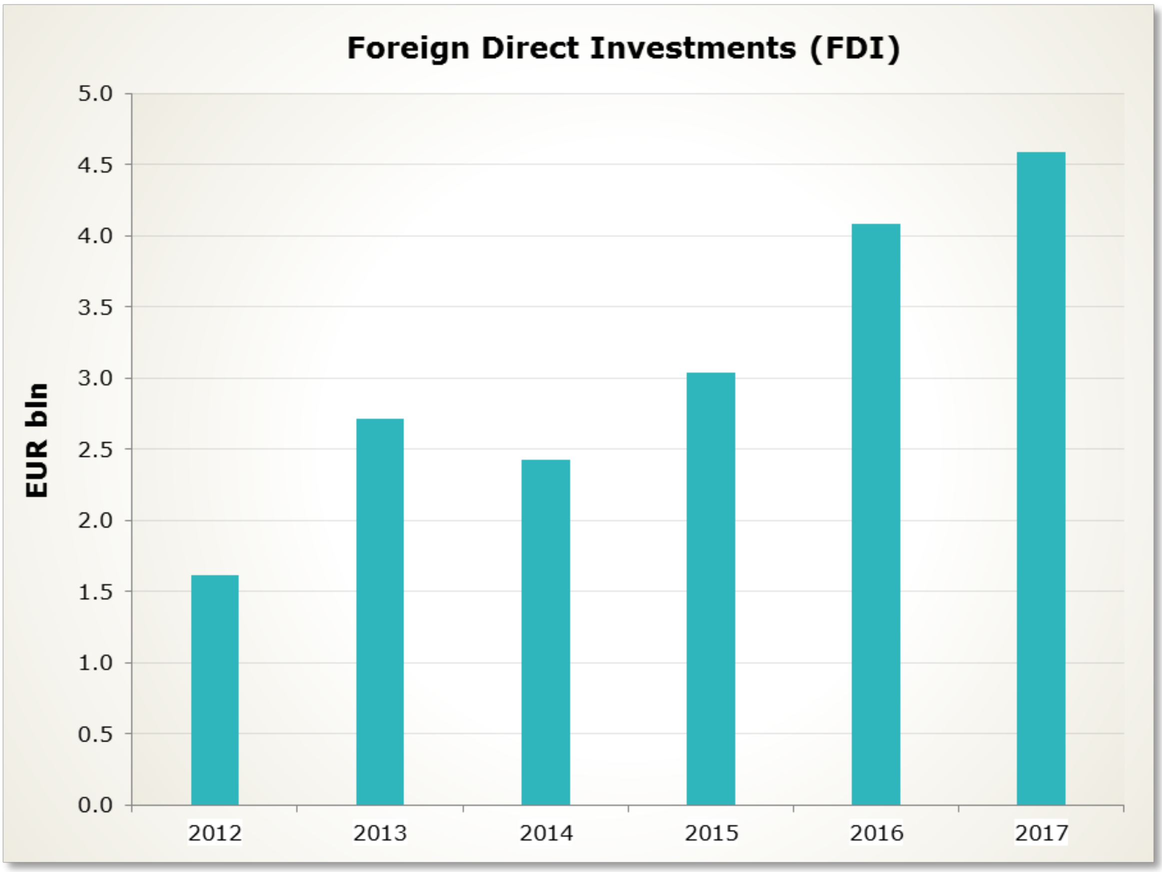


Source: NBR

7.3. FDI

Net FDI grew by 12.4% y/y in 2017

Foreign direct investments (FDIs) in Romania totalled EUR 4.6 bln in 2017, according to NBR. The FDIs increased by 12.4% compared to 2016. In 2016, FDIs advanced by 35% y/y to EUR 4.0 bln.



Source: NBR

7.4. FOREIGN TRADE

Foreign trade deficit widened by 28% in 2017

The trade deficit extended to EUR 11.9 bln in 2017, compared to EUR 9.3 bln in 2016, according to NBR.

Imports grew faster than exports – by 12%, totalling EUR 69 bln. Exports rose by 9.6%, totalling EUR 57.2 bln.

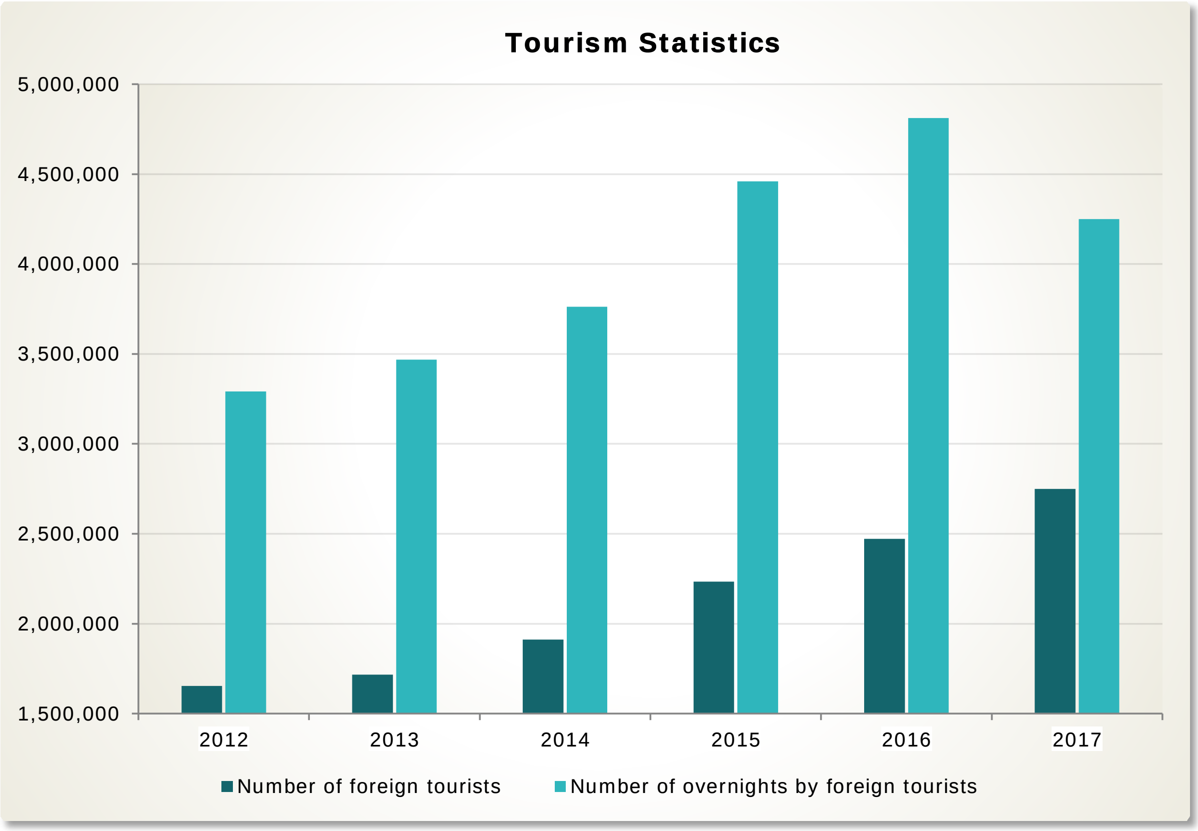
Source: NBR

7.5. TOURSIM

Number of foreign tourist overnights grew by 11.7% y/y in 2017

Tourist overnights of foreigners increased by an annual 11.7% to 4.25 million in 2017, according to INSSE data. The number of foreign tourists also went up – by 11% y/y to 2.75 million. Germany led the ranking in terms of number of tourists in the period – 121,795, followed by Israel with 103,365 tourists and Italy with 74,509.

The share of foreign tourist overnights in the total number of overnights was 16% in the fourth quarter of 2017, or by 1.0 pp more than in the year-ago quarter.



Source: INSSE

8. MAJOR DEVELOPMENTS

Romania's RON ends 2017 at fresh all-time low
Dec 29, 2017
The Romanian leu (RON) weakened to an all-time low against the euro amid unrest caused by protests against government plans to introduce controversial changes to the judicial system.
Read the full story here

EU backs Romania with EUR 86.6 mln to improve access to drinking water
Dec 20, 2017
The European Commission is providing a total of EUR 86.6 mln to help Romania improve access to drinking water.
Read the full story here

EBRD to help Romania develop priority infrastructure projects
Dec 8, 2017
The European Commission is providing a total of EUR 252 mln to help Romania improve its road and water infrastructure.
Read the full story here

Loose fiscal policy, lack of reform poses risks for Romania's growth prospects - Moody's

Nov 24, 2017

Moody's Investors Service announced that although Romania has made material progress in correcting macroeconomic imbalances, these improvements could be eroded in the medium-term due to a loose fiscal policy and lack of reform.

Read the full story here

Romania's share of organic farming area second lowest in EU

Nov 16, 2017

Romania's organic farming area as a percentage of total crop area in the country was the second lowest in the European Union in 2016, according to the Eurostat.

Read the full story here

Share of people employed in agriculture in Bulgaria, Romania highest in EU – Eurostat

Nov 8, 2017

In 2015, Romania and Bulgaria had the highest share of population employed in the agriculture sector among EU member states, the bloc's statistical institute Eurostat, announced in December 2017.

Read the full story here

EIB, Romania's UniCredit Bank sign EUR 50 mln loan deal

Nov 6, 2017

The European Investment Bank (EIB) signed a EUR 50 mln loan agreement with Romania's UniCredit Bank under the European Fund for Strategic Investments (EFSI). UniCredit Bank will use the loan to finance innovative or riskier projects by SMEs, mid-caps, start-ups and companies promoting employment in general and jobs for the young people in particular.

Read the full story here

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