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# Weekly Report

## Romania

22 August 2012



## Tight liquidity keeps the leu up; CC's decision offers further support

### Macroeconomics: Q2 GDP up by 1.2% YoY and 0.5% QoQ (Page 3-4)

Q2 GDP growth data (+1.2% YoY and 0.5% QoQ, SA) came out better than analysts' expectations of 1% YoY and 0.2% QoQ (Reuters poll). This was the first positive rate after two consecutive negative quarters. By comparison, in the EU17 and EU27 we witnessed a 0.2% QoQ decline. Looking forward, agriculture will weigh down on Q3 and Q4 GDP but we expect positive contribution from commerce, given the increased wages of the public sector employees. Industrial production prospects in Q3 are not good, especially since we saw a clear slowdown in May and June (seasonally adjusted data). Also, prospects in constructions are deteriorated, especially since public expenditure has to be carefully watched while in the case of the private sector there is little support to finance this type of business as demand for the real estate has not picked up yet. During the first 6M the CA deficit shrank further, by 29.5% YoY, to 2.4 bn EUR. On the positive side, the financing side of the CA deficit improved.

### FX markets: leu remains strong for the moment (Page 5)

For the moment, the leu is still under the influence of the liquidity squeeze operated by the Central Bank. Also supportive for the leu was the better than expected GDP data for Q2 2012: GDP grew by 1.2% YoY (+0.5% QoQ) compared to analysts' expectations of 1% YoY (0.2% QoQ). Moving further, the IMF's sixth evaluation of the standby agreement came out also positive. To the above events, we add the fact that the deadline for the final ruling on the validity of the referendum by the Constitutional Court was brought closer to 21<sup>st</sup> August from 31<sup>st</sup> August. The CC decided yesterday that the quorum was not met, so the vote is invalid. While committed to follow CC's decision, we expect new actions to be taken by the USL to remove the President and the tension between the PM and Mr. Basescu to continue. Also, we believe the liquidity cap will be temporary and that risks for the leu are tilted towards depreciation from the current levels.

### Government securities: yields continue to advance (+31 bp WoW for the 12M T-bills) (Page 6-7)

The yield curve has shifted up significantly in the past two weeks, especially at the low end of the curve. T-bills yields (12M) were higher by 42bp WoW last Thursday and the spread to German bunds widened some 14 bp to 640 bp in the case of 3Y bonds. The 5Y CDS is at relatively lower levels (366 bp) compared to the end of May. There was only one auction last week for 8M T-bills, with an average planned amount 700 mn RON. The entire sum was sold at an average accepted yield of 5.91%.

### MM: repo volume diminishes again (Page 8-9)

Last week, the Central Bank continued to preserve the cap on liquidity and injected only 5bn RON at the weekly repo, lower by 1 bn RON than the previous week. The transmission of higher MM rates already started to feed into the loan rates applied to corporations, the segment which had the best evolution so far this year in terms of lending (2.5% YTD in June compared to 1.1% YTD in the case of households) and for which the weight of loans denominated in RON is quite significant at 40%. Therefore, in June, when average ROBOR 3M stood at 5.35% (41 bp higher than in May) the average RON interest rate for new loans for companies increased by 18 bp to 9.52%. In August, the average ROBOR 3M advanced by another 20 bp to 5.65%.

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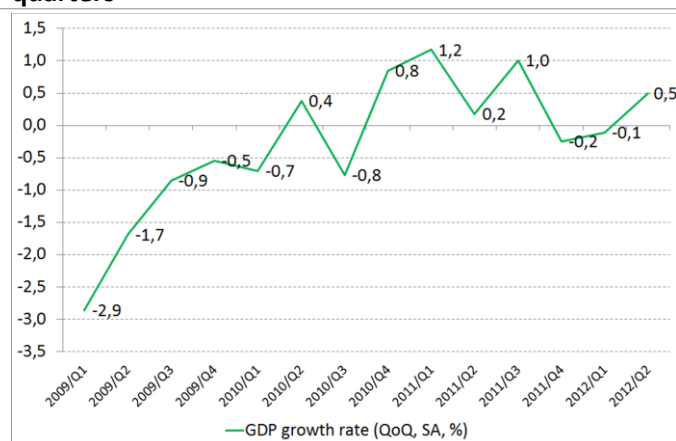
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**Macroeconomics: Q2 GDP up by 1.2% YoY and 0.5% QoQ**

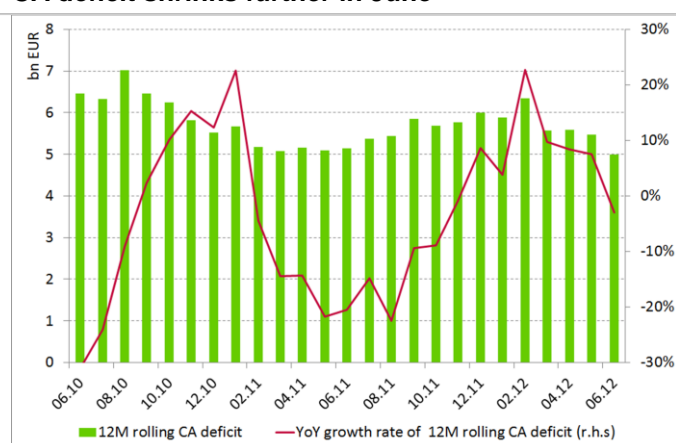
	PERIOD	INDICATOR	FACT	CONSENSUS	PRIOR
13 Aug	June	CA balance (EUR mn, YTD)	-2.411		- 1.920
14 Aug	Q2 2012	Flash GDP growth rate ( q-o-q, %, seasonally adjusted)	0,5	0,2	-0,1
24 Aug	July	M3 aggregate (y-o-y, %)			8,5
24 Aug	July	Non -governmental loans (y-o-y, %)			6,3
24 Aug	July	Non -governmental deposits (y-o-y, %)			9,6

**Q2 GDP growth data (+1.2% YoY and 0.5% QoQ, SA) came out better than analysts' expectations of 1% YoY and 0.2% QoQ (Reuters poll). This was the first positive rate after two consecutive negative quarters. By comparison, in the EU17 and EU27 we witnessed a 0.2% QoQ decline.** These results in domestic data are due especially to extraordinary growth rate recorded by constructions in Q2 2012, supported by public expenditure with infrastructure works. In 2011, constructions value added (VA) represented 9.8% of the GDP, while industry's VA was 26.3%, wholesale and retail trade VA 19% and agriculture's VA was 6.5% of the GDP. The detailed GDP data will be published on 6<sup>th</sup> September.

Looking forward, agriculture will weigh down on Q3 and Q4 GDP but we expect positive contribution from commerce, given the increased wages of the public sector employees. Industrial production prospects in Q3 are not good, especially since we saw a clear slowdown in May and June (seasonally adjusted data) and prospects for July are negative as pointed by ESI (the economic sentiment indicator). Given that a significant side of demand for manufactured goods comes from the eurozone, we also add the decreasing pace of exports which marked a negative annual growth rate in June after two consecutive months of growth. Also, prospects in constructions are deteriorated, especially since public expenditure has to be carefully watched while for the private sector there is little support to finance this business as demand for real estate has not picked up yet.

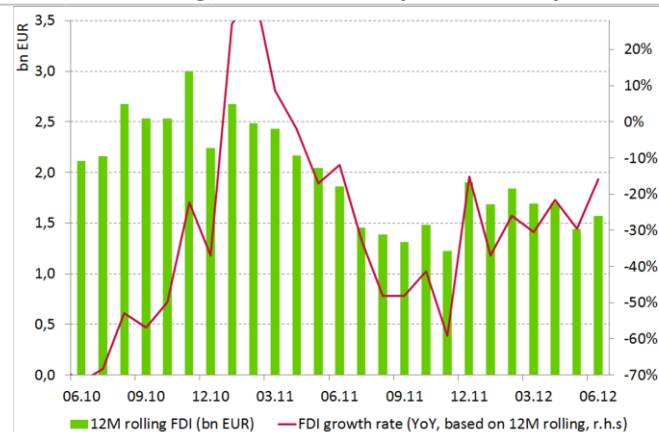
**GDP growth resumes in Q2 2012 after two negative quarters**


Source : NIS, OTP Research

**CA deficit shrinks further in June**


Source : NBR, OTP Research

During the first 6M the CA deficit shrank further, by 29.5% YoY, to 2.4 bn EUR. Main influence came from incomes' balance where the deficit shrank by 524 mn EUR (-31% YoY). Also, a positive impact came from the diminishing trade gap (by 257 mn EUR or -7.5% YoY) and higher surplus in current transfers (by 225 mn EUR or +13.4% YoY). In the case of incomes' balance, the result is mainly due to a sharp drop in the deficit of the income balance from direct investments which probably means that return on investment in Romanian assets has decreased significantly this year. This evolution is true in the case of portfolio investments as well (including Government securities). On the positive side, the financing side of the CA deficit improved: FDI financed 24.2% of the CA deficit and during the first 6M they were 585 mn EUR, lower by 36% YoY whereas during the first 5M they were lower by 52% YoY.

**FDI (12M rolling) increased compared to May**


Source : NBR, OTP Research

## Medium-term macroeconomic forecast

Main macroeconomic indicators	Fact						Forecast	
	2006	2007	2008	2009	2010	2011	2012	2013
Real GDP	7,9%	6,3%	7,3%	-6,6%	-1,6%	2,5%	1,4%*	2,8%*
Final consumption of households	12,9%	12,0%	9,0%	-10,4%	-0,4%	1,4%	2,3%	2,9%
Households consumption expenditure	12,7%	11,9%	9,0%	-10,1%	-0,4%	1,3%		
Government consumption	-11,5%	2,5%	6,2%	9,5%	-10,0%	-3,4%	-0,7%	1,7%
Gross fixed capital formation	19,9%	30,3%	15,6%	-28,1%	-2,1%	6,3%	5,2%	6,2%
Exports	10,4%	7,8%	8,3%	-6,4%	14,0%	9,9%	3,3%	8,4%
Imports	22,6%	27,3%	7,9%	-20,5%	11,9%	10,5%	4,2%	8,8%
Consumer prices (avg.)	6,6%	4,8%	7,8%	5,6%	6,1%	5,8%	3,5%	3,0%
Budget Balance (GDP%, ESA 95)	-2,2%	-2,9%	-5,7%	-9,0%	-6,8%	-5,2%	-3,6%	-3,3%
Public debt (GDP %)	12,4%	12,8%	13,4%	23,6%	31,0%	33,3%	35,3%	36,7%
CA balance (% GDP)	-10,5%	-13,4%	-11,6%	-4,2%	-4,4%	-4,2%	-4,4%	-4,6%
CA balance (bn EUR)	-10,2	-16,8	-16,2	-4,9	-5,5	-5,7	-6,0	-6,4
Unemployment	7,3%	6,4%	5,8%	6,9%	7,3%	7,4%	6,8%	6,6%
Nominal wage growth	18,4%	21,8%	26,1%	4,8%	3,1%	6,5%**	4,5%	4,4%
Real wage growth	9,0%	14,7%	16,5%	-1,5%	-3,7%	0,5%**	1,0%	1,4%
Key interest rate (avg.)	8,6%	7,5%	9,7%	9,1%	6,5%	6,2%	5,33%	5,25%
Key interest rate (e.o.p.)	8,8%	7,5%	10,3%	8,0%	6,3%	6,0%	5,25%	5,25%
EUR/RON (avg.)	3,52	3,34	3,68	4,24	4,21	4,24	4,44	4,60
EUR/RON (e.o.p.)	3,38	3,61	3,99	4,23	4,28	4,32	4,50	4,59

Source: Eurostat, OTP Research

Note: \*under revision; \*\* forecast

**FX markets: leu remains strong for the moment**

For the moment, the leu is still under the influence of the liquidity squeeze operated by the Central Bank. Also supportive for the leu was the better than expected GDP data for Q2 2012: GDP grew by 1.2% YoY (+0.5% QoQ) compared to analysts' expectations of 1% YoY (0.2% QoQ). Moving further, **the IMF's sixth evaluation of the standby agreement came out also positive**, despite of the lowering of the expected GDP growth for 2012. No specific austerity measures were announced to keep down the budget deficit so altogether the impact of the evaluation was positive. To the above events, we add the fact that **the deadline for the final ruling on the validity of the referendum by the Constitutional Court was brought closer to 21<sup>st</sup> August** from 31<sup>st</sup> August (the first announced date being 12<sup>th</sup> September).

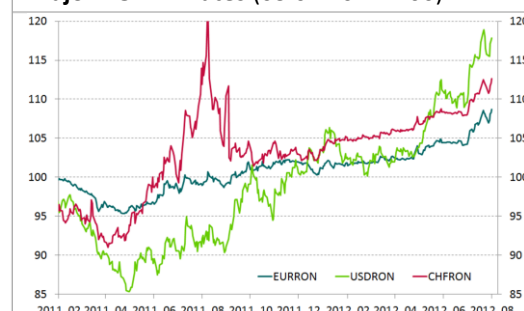
Meanwhile, in Europe there is a marginally improved sentiment regarding the steps expected to be taken to solve the debt crisis and risk aversion is at lower levels. Investors are optimistic about next ECB move and wait for more clear measures to be announced on 6<sup>th</sup> September at the monthly ECB policy meeting.

In the past two months however, the most significant impact on the leu was due to domestic events and the current political tensions do not seem to end. The Constitutional Court decided yesterday that the quorum was not met, so the vote is invalid. While committed to follow CC's decision, we expect new actions to be taken by the USL to remove the President and the tension between the PM and Mr. Basescu to continue. Also, as shown in the previous report, we believe the liquidity cap will be temporary and that risks for the leu are tilted towards depreciation from the current level.

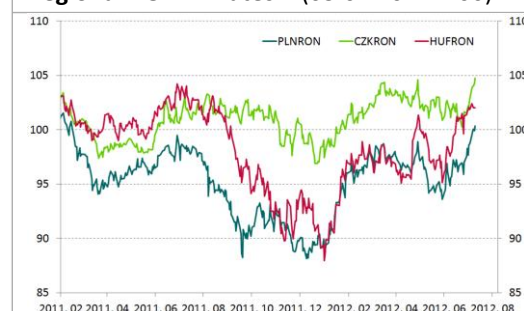
Last data: 16.08.2012

FX BID				
	Value		Weekly chg. (%)	YTD chg. (%)
EURRON	4,48	↓	-1,33	↑ 3,65
USDRON	3,62	↓	-1,75	↑ 8,78
CHFRON	3,73	↓	-1,30	↑ 5,03
RONJPY	4,57	↓	-2,76	↑ 5,48
RONPLN	1,10	↓	-1,37	↑ 7,11
100HUFRON	1,61	↓	-1,83	↑ 17,83
RONCZK	0,18	↓	-0,44	↑ 7,01
RONRUB	0,11	↓	-2,22	↑ 10,02
RONRSD	0,04	↓	-1,88	↓ -5,78
RONBGN	2,29	↓	-1,37	↑ 3,89

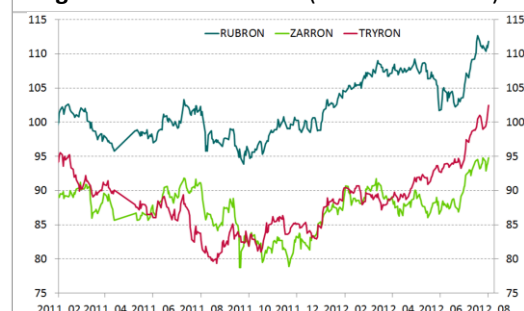
Source: Reuters

**Major RON FX rates (03.01.2011=100)**


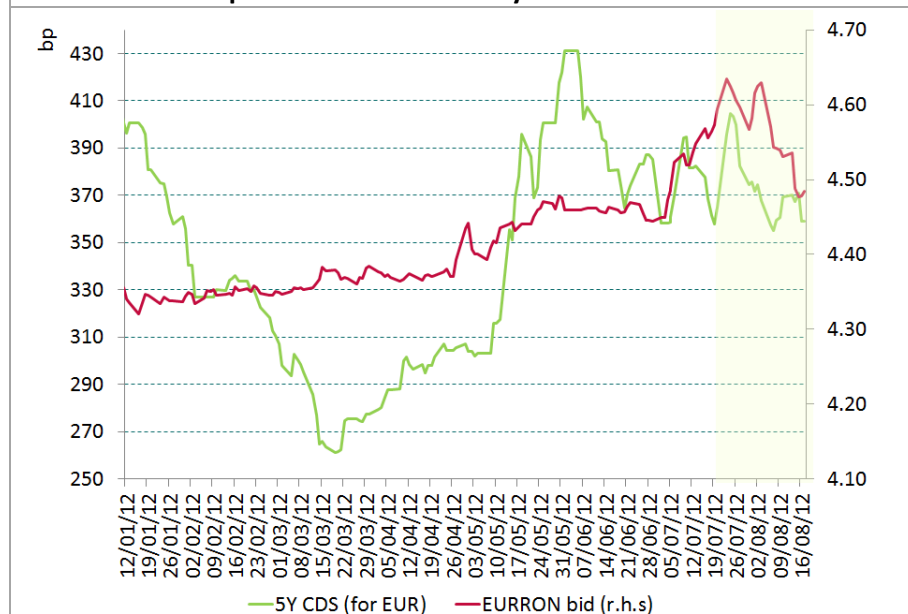
Sources: Reuters, OTP Research

**Regional RON FX rates I. (03.01.2011=100)**


Sources: Reuters, OTP Research

**Regional RON FX rates II. (03.01.2011=100)**


Sources: Reuters, OTP Research

**The leu grew stronger due to liquidity squeeze; the CDS is at relatively lower levels compared to the end of May**


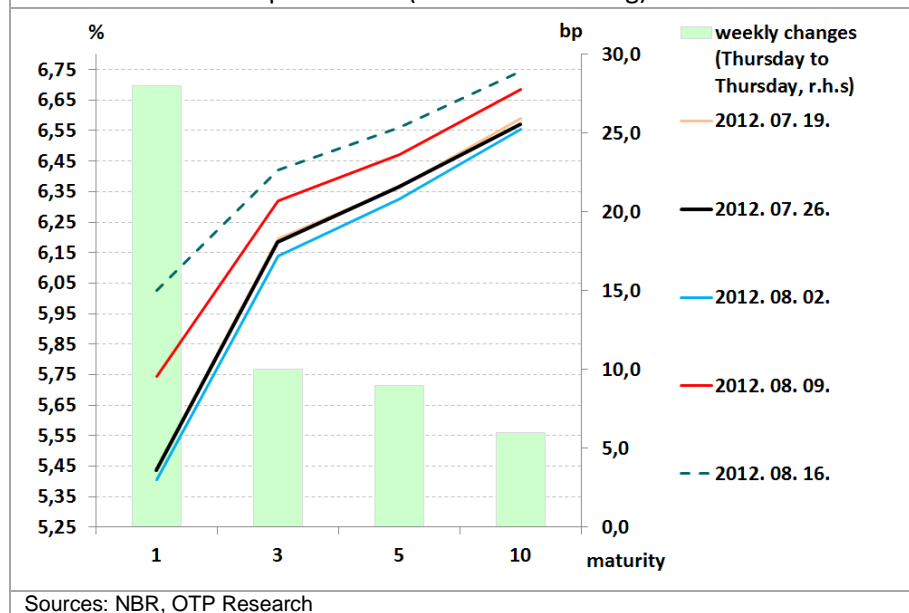
Sources: Reuters, OTP Research

## Government securities: yields continue to advance (+31 bp WoW for the 12M T-bills)

The yield curve has shifted up significantly in the past two weeks, especially at the low end of the curve. T-bills yields (12M) were higher by 42bp WoW last Thursday and the spread to German bunds widened some 14 bp to 640 bp in the case of 3Y bonds. The 5Y CDS is at relatively lower levels (366 bp) compared to the end of May.

For the moment, yields are driven by the evolution of the money market rates and there is little impact from domestic or external events which could modify risk perception. The Central Bank's decision to cap liquidity maintains the upward pressure on the yields.

Yield curve over the past weeks (Central Bank fixing)

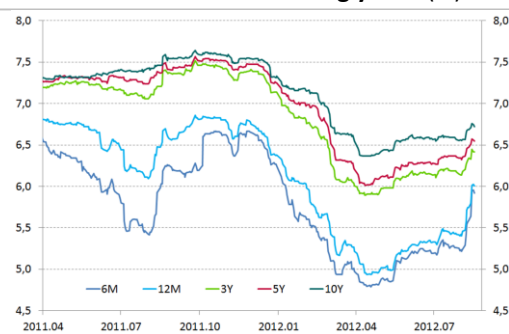


Last data: 16.08.2012

RON GOVERNMENT SECURITIES				
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)	
6M	5,96	↑ 42,0	↓ -29	
12M	6,03	↑ 31,0	↓ -36	
3Y	6,42	↑ 13,5	↓ -72	
5Y	6,56	↑ 10,5	↓ -69	
10Y	6,75	↑ 7,5	↓ -59	
SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
GERROM 3Y	640	↑ 14,0	↓ -46	
GERROM 5Y	616	↑ 10,9	↓ -34	
GERROM 10Y	531	↑ 7,5	↓ -20	
3Y -5Y	14	↓ -3,0	↑ 3	
5Y -10Y	19	↓ -3,0	↑ 11	
3Y-10Y	33	↓ -6,0	↑ 14	
FLY 3-5-10	4	↓ 0,0	↑ 7	
CDS MID SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
3Y EURO	316	↑ 5,8	↓ -56	
5Y EURO	366	↑ 5,7	↓ -36	

Source: Reuters

Central bank benchmark fixing yields (%)



Sources: NBR, OTP Research

Slope of the yield curve (bp)



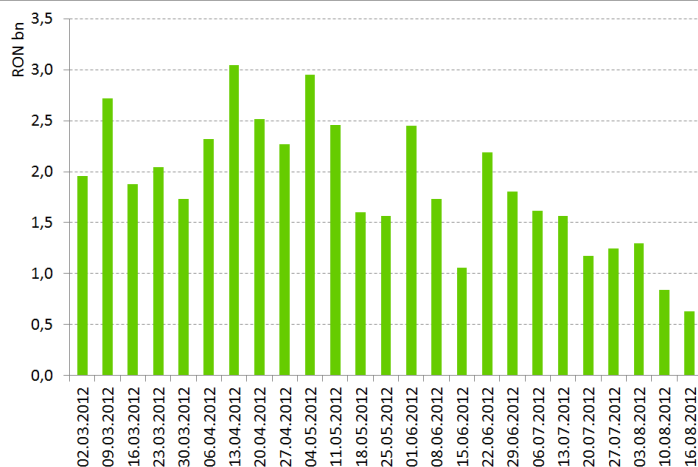
Sources: NBR, OTP Research

FLY 3-5-10 (bp)



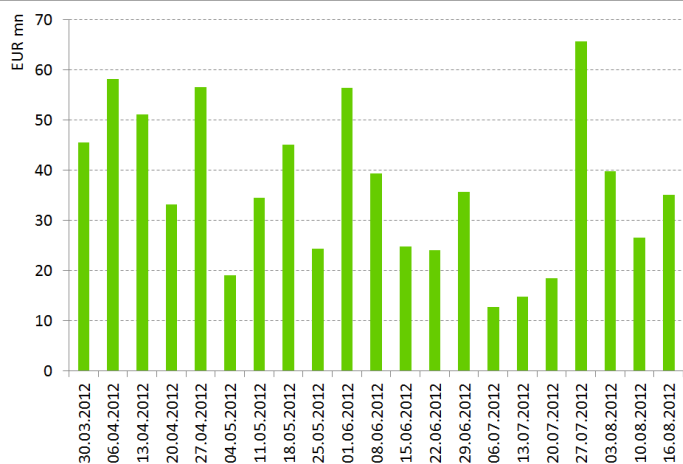
Sources: NBR, OTP Research

**RON denominated securities (avg. daily volume) traded on the secondary market (without NBR) continuously dropping**



Sources: NBR, OTP Research  
Note: the average for the last week does not include Friday;

**EUR denominated securities (avg. daily volume) traded on the secondary market (without NBR) rose last week**

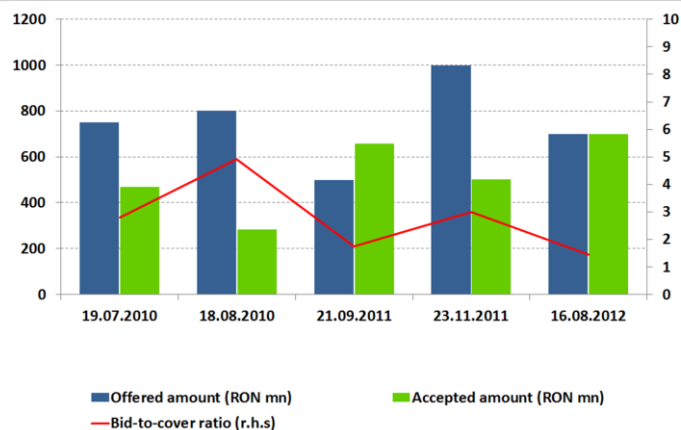


Sources: NBR, OTP Research  
Note: the average for the last week does not include Friday;

**Auctions**

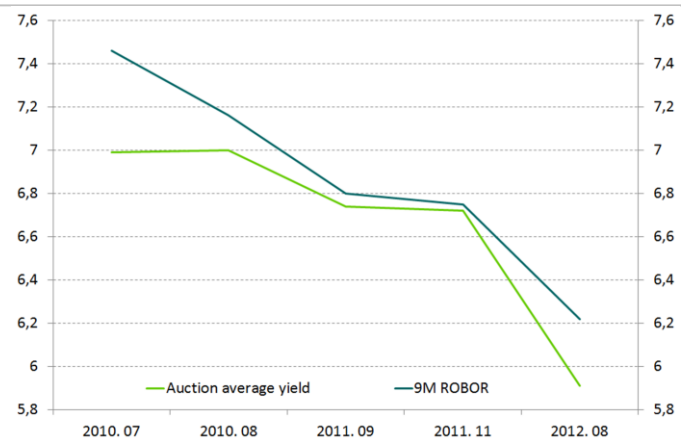
There was only one auction last week for 8M T-bills, with an average planned amount 700 mn RON. The entire sum was sold at an average accepted yield of 5.91%. The last similar auction was held in the end of November last year, for 9M T-bills and the average accepted yields stood at 6.72%. Since then, the base rate dropped by 75 bp. Bid to cover ratio was relatively low at 1.45.

**9M auctions data**



Sources: NBR, OTP Research

**9M interest rates**



Sources: NBR, OTP Research

**Results of last week's auction**

RO1213CTN0G4	
Offered amount (RON mn)	700
total bids (RON mn)	1018
accepted amount (RON mn)	700
average accepted yield (%)	5,91
coupon	-

Sources: NBR, OTP Research

**T-bills auction in August**

ISIN	Auction date	Settlement date	Maturity	Months	Indicative target amount (RON)
RO1213CTN0F6	06.08.2012	08.08.2012	07.08.2013	12	700.000.000
RO1213CTN0G4	13.08.2012	16.08.2012	24.04.2013	8	700.000.000
RO1213CTN0H2	20.08.2012	22.08.2012	21.08.2013	12	500.000.000

Source: Ministry of Finance, OTP Research

**Bonds auctions in August**

ISIN	Auction	Settlement	Maturity	Years	Cupon %	Indicative target amount (RON)
RO1214DBN068	09.08.2012	13.08.2012	28.07.2014	2	5,85	400.000.000
RO1216DBN030	23.08.2012	27.08.2012	27.01.2016	4	5,75	200.000.000

Sources: Ministry of Finance, OTP Research

**The MinFin decreased the weight of bonds issue in August**

	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12	Jul-12	Aug-12
Planned targeted amount (RON bn)	4,5	5,0	5,0	4,3	3,8	3,5	2,3	2,5
% of bonds	33%	44%	54%	76%	80%	49%	69%	24%

Source: Ministry of Finance, OTP Research

**MM: repo volume diminishes again**

Last week, the Central Bank continued to preserve the cap on liquidity and injected only 5bn RON at the weekly repo, lower by 1 bn RON than the previous week. The offered amount stood at 18 bn RON, higher by 3bn than the previous week. **Consequently, the rates continued to advance and the weekly jump was 40-60 bp on Thursday. Therefore, with few exceptions (1M and 3M) they reached higher by almost 100 bp than the base rate.** If the cap persists after the end of the observation period for the required reserves (23<sup>rd</sup> August) rates are likely to remain decoupled from the base rate.

ROBOR 3M, the benchmark to which most loan contracts are linked to has been below the base rate by maximum 100bp (considering ROBOR 3M's monthly average) since January 2011 and only this year in June it climbed above the base rate: by 10 bp in June and July and 40 bp in August. **The transmission of higher MM rates already started to feed into the loan rates applied to corporations, the segment which had the best evolution so far this year in terms of lending (2.5% YTD in June compared to 1.1% YTD in the case of households) and for which the weight of loans denominated in RON is quite significant: 40%, higher than in the case of households where RON denominated loans represent only 33% of total loans.** Therefore, in June, when average ROBOR 3M stood at 5.35% (41 bp higher than in May) the average RON interest rate for new loans for companies increased by 18 bp to 9.52%. In August, the average ROBOR 3M advanced by another 20 bp to 5.65%.

**We emphasize the importance of RON denominated loans for companies by pointing to the fact that the majority of these loans are working capital loans, that companies use just to keep the business going.** So, 59% of the RON denominated loans (for companies) are below one year and another 21% are loans with a maturity from 1 to maximum 5 years. The higher costs can lead to lower profitability for companies given that they probably find it difficult to pass these costs to clients due to weak demand. Ultimately, it hurts economic growth as businesses downsize.

**On the other hand, the non performing loans ratio (90+ DPD) advanced quite rapidly this year as the leu depreciated against the euro: from 14.33% in December 2011 to 16.76% in June.** The capital adequacy ratio was at good levels though in June, 14.66%, significantly above the 10% level established by NBR following discussions with the IMF. To continue, the Central Bank is worried about inflation pressures as well and also by the fact that the weaker leu finally feeds into export prices too because a significant part of imports are incorporated into exported products.

As we said in a previous report, we believe that the existence and deepening deficit of liquidity, increase in treasury's yields and the incentive to save instead of consuming will determine the CB to end this cap on liquidity well before the end of the year.

Last data: 16.08.2012

MID INTEREST RATES			
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)
repo rate	5,25	↔ 0	↓ -75
ROBOR ON	6,22	↑ 60	↑ 169
ROBOR 3M	6,05	↑ 40	↔ 0
ROBOR 6M	6,22	↑ 42	↓ -31
ROBOR 9M	6,22	↑ 43	↓ -39
ROBOR 1Y	6,22	↑ 41	↓ -44

REPO			
	Value (mn RON)	Wly chg. (mn RON)	YTD chg. (mn RON)
repo amount	4.999,3	-1000,5	-1711,7

INTERBANK DEPOSITS			
	Value (mn RON)	Wly chg. (mn RON)	YTD chg. (mn RON)
outstanding	3.213,4	391,8	-814,1

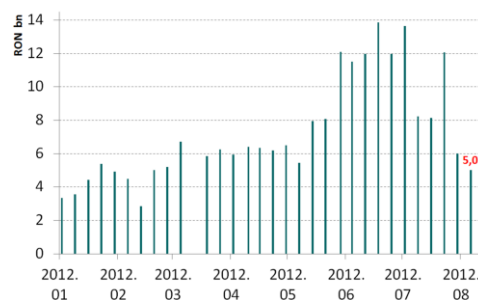
  

MID SWAP POINTS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
USD RON 1W	41	↑ 4	↑ 16
USD RON 1M	179	↑ 22	↑ 29
USD RON 3M	500	↑ 16	↑ 253
EUR RON 1W	45	↓ -1	↑ 5
EUR RON 1M	215	↑ 19	↑ 69
EUR RON 3M	607	↓ -20	↑ 96

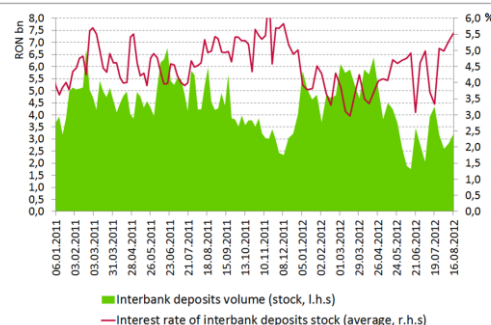
  

MID EUR BASIS SWAPS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
EUR RON 1Y	-60	↔ 0	↑ 95
EUR RON 3Y	-60	↔ 0	↑ 95
EUR RON 5Y	-55	↔ 0	↑ 95

Source: Reuters

**Repo operations during 2012**


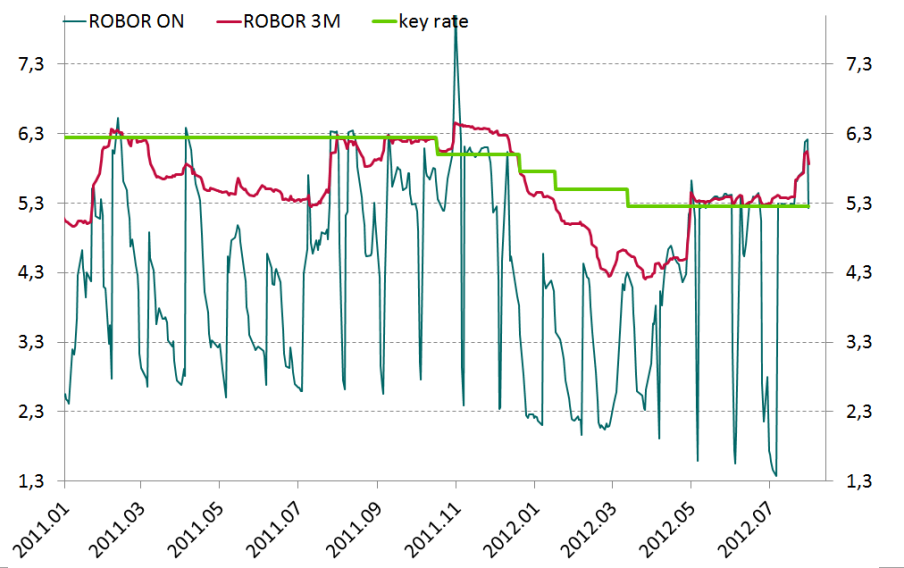
Sources: NBR, OTP Research

**Interbank deposits stock and average interest rate**


Sources: NBR, OTP Research



**Most important MM instruments from 2011 (%)**



Sources: NBR, OTP Research

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