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Weekly Report

Romania

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Future monetary policy easing under the radar

Macroeconomics: In Q1, industry rose by 4.7% YoY, retail trade stagnated and constructions fell by 4.1% YoY (Page 3-4)

In the first quarter, the annual dynamics of the business cycle indicators was mixed: industrial production rose by 4.7% YoY, retail trade stagnated (+0.1% YoY) and construction works declined by 4.1% YoY. According to the April survey published by NBR, Q2 starts well in constructions and production so short term prospects are good. In March alone, constructions' annual dynamics was positive for the first time this year (+1% YoY and +2.7% MoM). The residential segment retreated 18% MoM after the unusual hike in February while infrastructure works (+8.6% MoM) and non-residential constructions (+3.7% MoM) enlivened the activity within the sector. Foreign trade dynamics revealed a weaker internal and external demand as imports dropped by 5% and exports by 1.4% (considering euro denominated figures). In Q1 exports exhibited a 4.6% YoY increase driven by the extra-EU trade where one third of the exports go.

FX markets: S&P affirmed Romania's BB+ rating (Page 5)

The leu lost 0.5% to the euro last week and the auction held by the Treasury on 9th of May did not seem to have attracted much interest from non-residents. The auction data coincided with the day in which S&P reaffirmed its rating for Romania. S&P is the only rating agency which still assigns the "junk" status to Romanian sovereign debt. At the latest press conference the NBR Governor supported the view that the current strengthening of the leu is in line with fundamentals: the CA deficit continued to shrink this year as well. However, the announced easing cycle of the interest rates, cumulated with the limited remaining upside potential for bond prices which determines non-residents' investment appetite makes us believe that the leu is less likely to reach new highs this year. Moreover, the large portfolio investments inflows recorded this year may be seen as a vulnerability and a potential source of volatility in the future.

Government securities: The yield curve shifted down significantly (Page 6-7)

The Treasury held two auctions last week to sell 6M T –bills and 5Y bonds. The average accepted yields were 4% and 4.45% respectively. The demand for the T-bills was high and bid to cover ratio mounted to 5.96 whereas the drop in yield was significant: -153 bp compared to the similar tender in January 2013. In the case of 5Y bonds, bid to cover was more modest, 1.89 and total subscriptions stood at 1.5 bn RON. The newly modified inflation forecast (by NBR) and the announced series of future rate cuts gives some more support for bond prices.

MM: The Central Bank announced a rate cut cycle (Page 8-9)

This week, the repo amount was negligible: 107 mn RON for 2 banks. For the moment, interest rates have fallen significantly below the base rate of 5.25%. At the last Board meeting, NBR kept the base rate at 5.25% and cut the interest corridor around it from +/- 4 pp to +/-3 pp in order to strengthen the transmission channel of the monetary policy. The CB also announced that a base rate cycle will start and lowered its inflation forecast for September and December 2013 by 0.3% to 3.2% YoY each. In light of new information, we expect two rate cuts this year, one in Q3 2013 and one in Q4, placing the base rate at 4.75% by the end of the year.

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Macroeconomics: In Q1, industry rose by 4.7% YoY, retail trade stagnated and constructions fell by 4.1% YoY

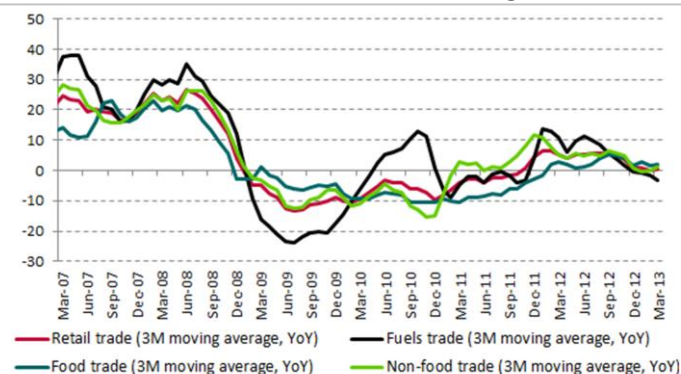
	PERIOD	INDICATOR	FACT	CONSENSUS	PRIOR
08 May	March	Producer Price Index (y-o-y, %)	4,5		5,4
08 May	March	Retail trade turnover index (y-o-y, %)	-3,5		1,6
10 May	March	Exports (y-o-y, %)	-1,4		10,1
10 May	March	Imports (y-o-y, %)	-5,0		1,3
13 May	March	Net wage growth rate (y-o-y, %)	4,8		5,5
13 May	March	Industrial trade turnover index (y-o-y, %)	-2,9		13,8
13 May	March	Index value of new orders in manufacturing (y-o-y, %)	0,7		15,8
13 May	March	Construction works index (y-o-y, %)	1,0		-5,7
14 May	March	Industrial Production Index (y-o-y, %)	1,3		7,2
15 May	March	CA balance (EUR mn, YTD)			327,4

In the first quarter, the annual dynamics of the business cycle indicators was mixed: industrial production rose by 4.7% YoY, retail trade stagnated (+0.1% YoY) and construction works declined by 4.1% YoY. To add to this picture, wages in the public sector are also higher compared to Q1 2012 and the number of employees adjusted much less, which means we should see a positive contribution to GDP coming from the public services as well. According to the April survey published by NBR, Q2 starts well in constructions and production so short term prospects are good.

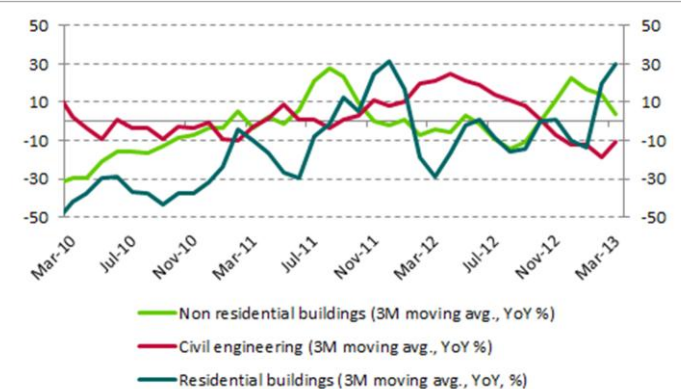
Taking a closer look to industrial production, it rose by 1.3% YoY and 0.3% (MoM, seasonally adjusted in March). The monthly rhythm has been low but positive since October 2012. The sales figure came down (-2.9% YoY) in March, due to lower domestic sales. In fact, domestic sales have been the weaker than foreign sales in Q1 2013, compared to Q1 2012. New orders' advance was much lower than in February (+0.7% YoY compared to 15.8% YoY).

In March, constructions' annual dynamics was positive for the first time this year (+1% YoY). The monthly uptake (+2.7% MoM, seasonally adjusted) was driven by new construction works. **The residential segment retreated 18% MoM after the unusual hike in February and infrastructure works (+8.6% MoM) and non-residential constructions (+3.7% MoM) enlivened the activity within the sector.** In Q1, the residential segment was marginally down (-1.1% QoQ), the non-residential strongly affected (-17.7% QoQ) and civil engineering posted a 4.8% QoQ hike.

Foreign trade dynamics revealed a weaker internal and external demand as imports dropped by 5% and exports by 1.4% (considering euro denominated figures). Exports had a better than expected pace in the first two months of the year and did not show weakness in spite of the leu's appreciation. In Q1 they exhibited a 4.6% YoY increase

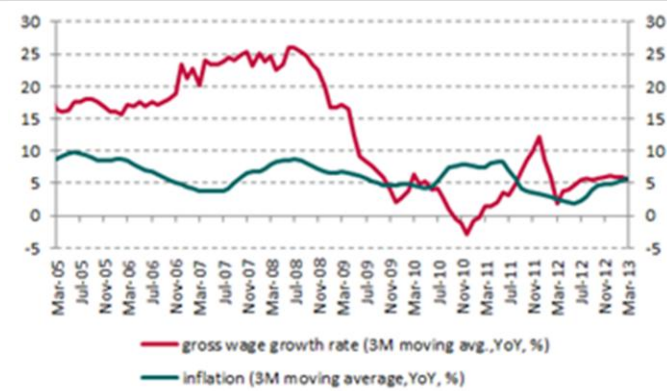
Fuels trade fell in Q1, but retail trade stagnated


Source: NIS, OTP Research

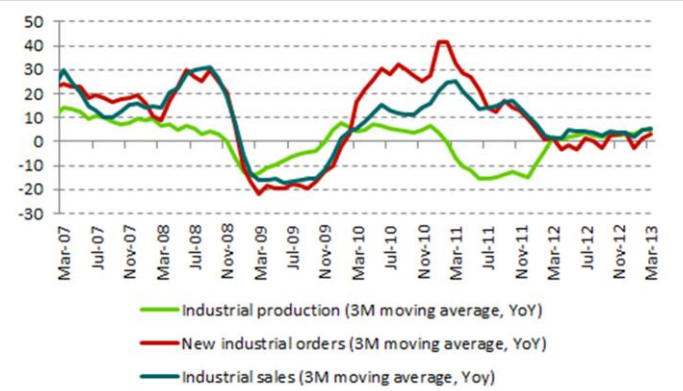
In Q1, the civil engineering works dragged down construction activity


Source: NIS, OTP Research

driven by non –EU trade (+10.9% YoY) which represents one third of total exports.

Gross average wage rose by 4.9% YoY; real wage down 0.4% YoY


Source: NIS, OTP Research

Industry rose by 4.7% YoY in Q1


Source: NIS, OTP Research

Medium-term macroeconomic forecast

Main macroeconomic indicators	Fact						Forecast	
	2007	2008	2009	2010	2011	2012	2013	2014
Real GDP	6,3%	7,3%	-6,6%	-1,1%	2,2%	0,7%	1,5%	2,6%
Households consumption expenditure	12,0%	9,0%	-10,4%	-0,2%	1,2%	1,0%	1,6%	2,5%
Government consumption	2,5%	6,2%	9,5%	-13,7%	-0,3%	2,4%	2,2%	1,5%
Gross fixed capital formation	30,3%	15,6%	-28,1%	-1,8%	7,3%	4,9%	0,9%	6,6%
Exports	7,8%	8,3%	-6,4%	13,2%	10,3%	-3,0%	-0,4%	3,2%
Imports	27,3%	7,9%	-20,5%	11,1%	10,0%	-0,9%	-0,3%	3,2%
Consumer prices (avg.)	4,8%	7,8%	5,6%	6,1%	5,8%	3,3%	4,9%	3,2%
Budget Balance (GDP%, ESA 95)	-2,9%	-5,7%	-9,0%	-6,8%	-5,6%	-2,9%	-2,8%	-2,5%
Public debt (GDP %)	12,8%	13,4%	23,6%	30,5%	34,7%	37,8%	38,7%	38,8%
CA balance (% GDP)	-13,4%	-11,6%	-4,2%	-4,4%	-4,5%	-4,0%	-3,5%	-4,0%
CA balance (bn EUR)	-16,8	-16,2	-4,9	-5,5	-5,9	-5,3	-4,9	-6,1
Unemployment	6,4%	5,8%	6,9%	7,3%	7,4%	7,1%	6,9%	6,5%
Nominal wage growth	21,8%	26,1%	4,8%	3,1%	4,1%	4,6%	5,0%	6,2%
Real wage growth	14,7%	16,5%	-1,5%	-3,7%	-1,9%	1,2%	0,1%	2,9%
Key interest rate (avg.)	7,5%	9,7%	9,1%	6,5%	6,2%	5,33%	5,13%	4,50%
Key interest rate (e. o. p.)	7,5%	10,3%	8,0%	6,3%	6,0%	5,25%	4,75%	4,50%
EUR/RON (avg.)	3,34	3,68	4,24	4,21	4,24	4,46	4,44	4,38
EUR/RON (e. o. p.)	3,61	3,99	4,23	4,28	4,32	4,43	4,41	4,34

Source: Eurostat, NBR, OTP Research

FX markets: S&P affirmed Romania's BB+ rating

The leu lost 0.5% to the euro last week and the auction held by the Treasury on 9th of May did not seem to have attracted much interest from non-residents. The auction data coincided with the day in which Standard and Poor's affirmed its rating for Romania. S&P is the only rating agency which still assigns the "junk" status to Romanian sovereign debt. S&P affirmed the BB+ rating for the long-term foreign and local currency and maintained the B rating for the short term local and foreign currency sovereign credit rating. The outlook was maintained stable. The agency argued in the press release that the reasons for the current status are the "low per capita GDP, developing institutions and vulnerability to external shocks owing to its still high, albeit declining external debt". Some investors probably hoped for a rating upgrade but considering the agency's explanations, the underlying weak points are structural and therefore will take some more time to adjust.

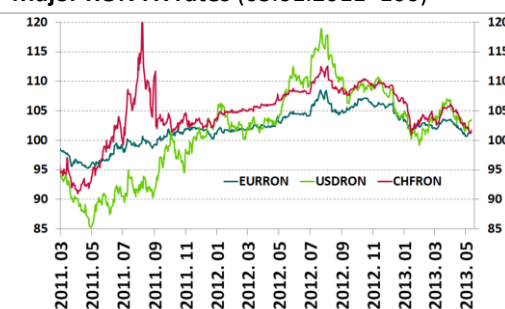
At the latest press conference the NBR Governor supported the view that the current strengthening of the leu is in line with fundamentals: the current account deficit continued to shrink this year as well after having adjusted in 2012 too. However, the announced easing cycle of the interest rates, cumulated with the limited remaining upside potential for bond prices which determines non-residents' investment appetite makes us believe that the leu is less likely to reach new highs this year. Moreover, the large portfolio investments inflows recorded this year may be seen as a vulnerability and a potential source of volatility in the future.

Last data: 10.05.2013

FX BID				
	Value		Weekly chg. (%)	YTD chg. (%)
EURRON	4,32	↑	0,49	↓ -2,71
USDRON	3,33	↑	1,49	↓ -1,15
CHFRON	3,48	↓	-0,81	↓ -5,47
RONJPY	3,27	↓	-1,10	↓ -15,60
RONPLN	1,04	↑	0,45	↓ -4,16
100HUFRON	1,47	↑	1,43	↓ -3,30
RONCZK	0,17	↓	-0,18	↓ -5,48
RONRUB	0,11	↑	0,59	↓ -3,68
RONRSD	0,04	↑	0,27	↓ -1,59
RONBGN	2,21	↑	0,60	↓ -2,65

Source: Reuters

Major RON FX rates (03.01.2011=100)



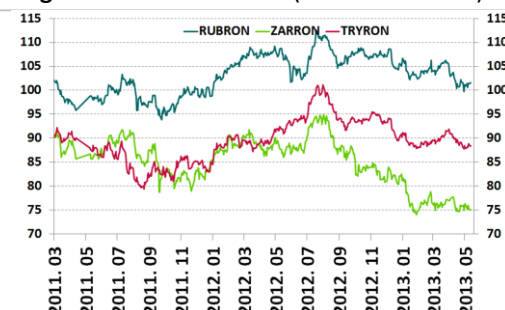
Sources: Reuters, OTP Research

Regional RON FX rates I. (03.01.2011=100)



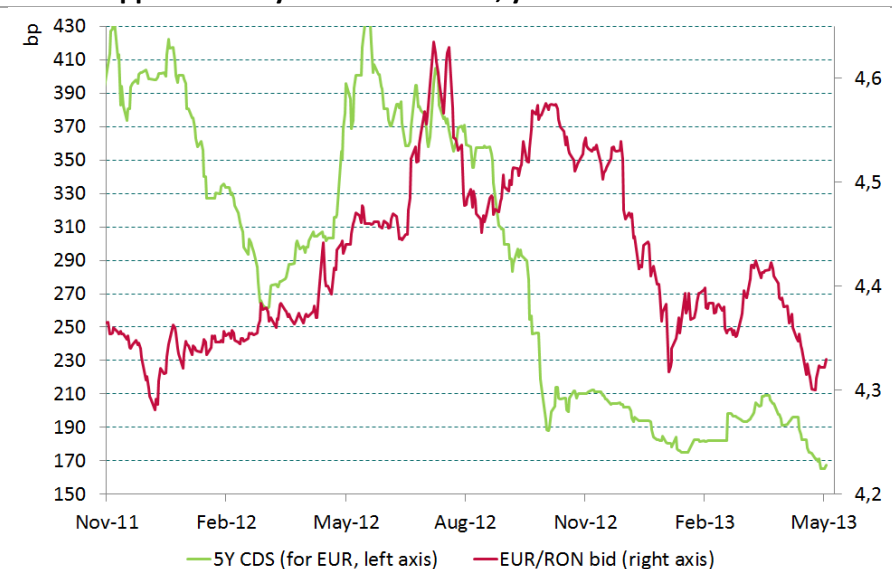
Sources: Reuters, OTP Research

Regional RON FX rates II. (03.01.2011=100)



Sources: Reuters, OTP Research

The leu appreciated by 2.7% to the euro, year to date



Sources: Reuters, OTP Research

Government securities: The yield curve shifted down significantly

The yield curve continued to shift down significantly last week (between 25 bp and 50 bp). This was in line with the decline seen by the money market rates. Since the beginning of the year, yields at the short end of the curve dropped by more than 200 bp. The 5Y CDS (euro contracts) stands at 165 bp and it is lower by 29 bp year to date. **The newly modified inflation forecast (by NBR) and the announced series of future rate cuts offers some more support to bond prices.**

The Treasury held two auctions last week to sell 6M T-bills and 5Y bonds. The average accepted yields were 4% and 4.45% respectively. The demand for the T-bills was high and bid to cover ratio mounted to 5.96 whereas the drop in yield was significant: -153 bp compared to the similar tender in January 2013. In the case of 5Y bonds, bid to cover was more modest, 1.89 and total subscriptions stood at 1.5 bn RON.

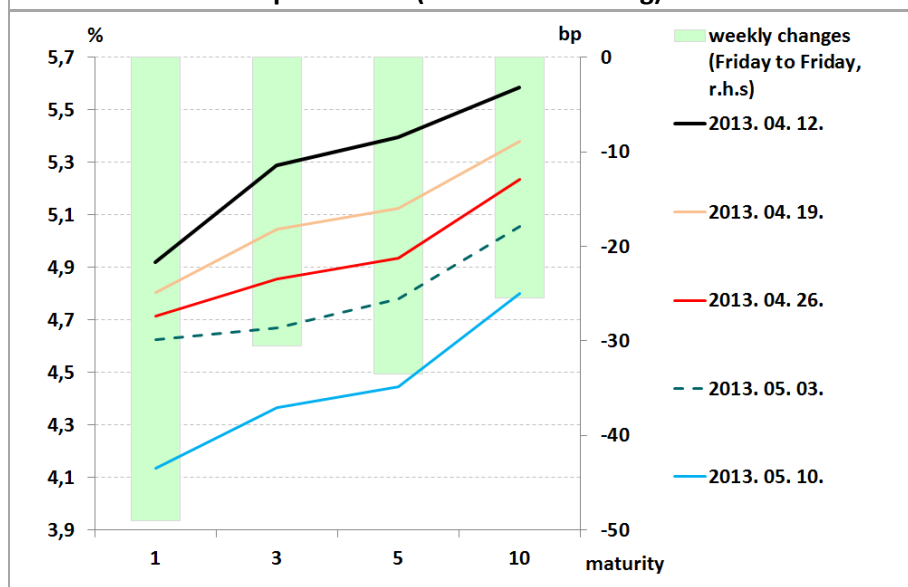
Last data: 10.05.2013

RON GOVERNMENT SECURITIES				
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)	
6M	4,01	↓ -44	↓ -218	
12M	4,14	↓ -49	↓ -203	
3Y	4,37	↓ -31	↓ -180	
5Y	4,45	↓ -33	↓ -176	
10Y	4,80	↓ -25	↓ -158	

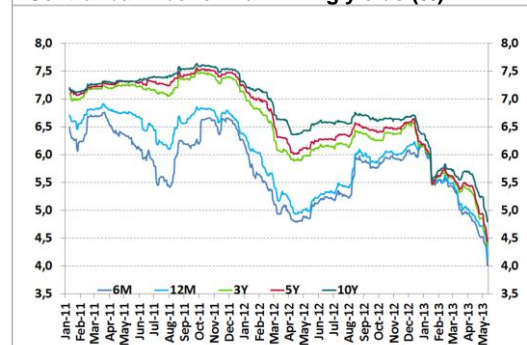
SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
GERROM 3Y	433	↓ -31	↓ -175	
GERROM 5Y	414	↓ -33	↓ -166	
GERROM 10Y	354	↓ -25	↓ -140	
3Y-5Y	8	↓ -3	↓ 4	
5Y-10Y	36	↑ 8	↑ 18	
3Y-10Y	44	↑ 5	↑ 22	
FLY 3-5-10	28	↑ 11	↑ 13	

CDS MID SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
3Y EURO	110	↓ -6	↓ -26	
5Y EURO	165	↓ -6	↓ -29	

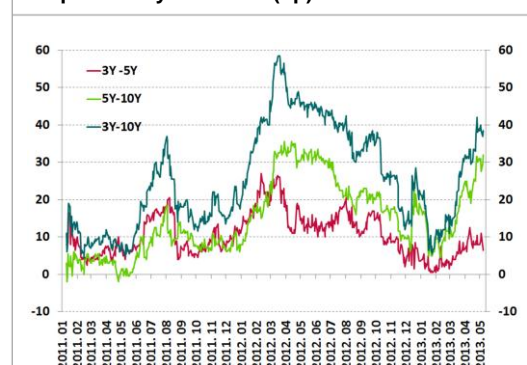
Source: Reuters

Yield curve over the past weeks (Central Bank fixing)


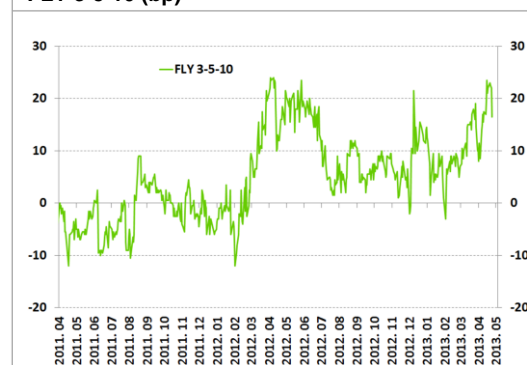
Source: NBR, OTP Research

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

T-Bills auctions in May (in RON)

ISIN	Auction date	Settlement date	Maturity	Months	Indicative target amount (RON)
RO1313CTN088	09.05.2013	13.05.2013	27.11.2013	6	500.000.000
RO1314CTN094	13.05.2013	15.05.2013	14.05.2014	12	800.000.000

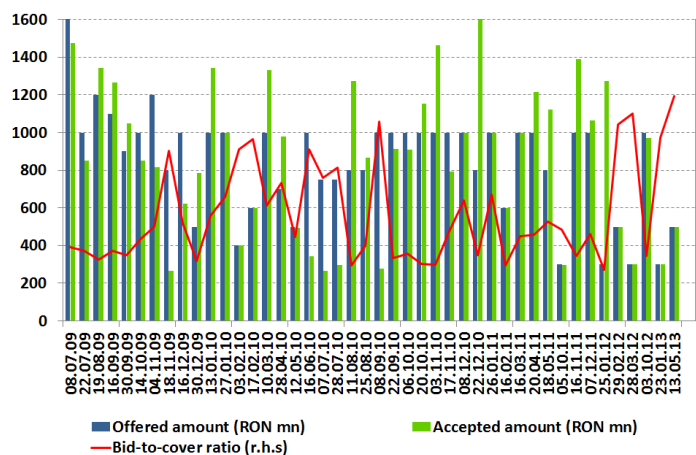
Source: Ministry of Finance, OTP Research

Bond auctions in May (in RON)

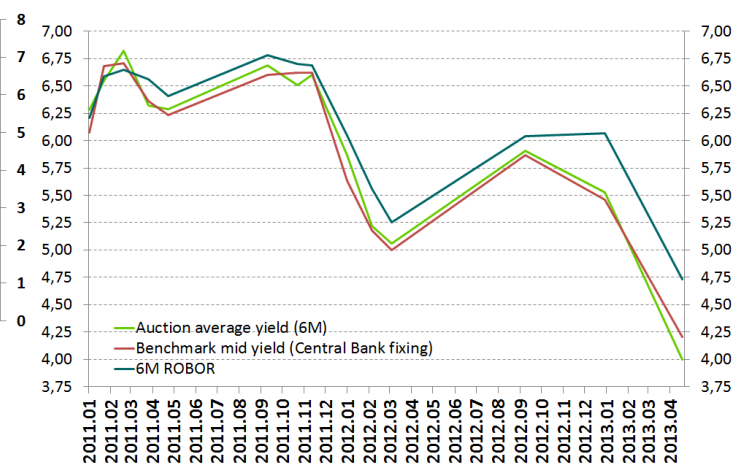
ISIN	Auction date	SSON auction date	Settlement date	Maturity	Years	Indicative target amount (RON)	Indicative target amount SSON* (RON)
RO1318DBN034	09.05.2013	-	13.05.2013	28.11.2018	5	800.000.000	-
RO1116DBN024	16.05.2013	17.05.2013	20.05.2013	30.04.2016	5	500.000.000	50.000.000
RO1217DBN046	20.05.2013	21.05.2013	22.05.2013	26.07.2017	5	300.000.000	30.000.000
RO1323DBN018	23.05.2013	-	27.05.2013	28.04.2023	10	600.000.000	-
RO1227DBN011	27.05.2013	-	29.05.2013	28.07.2027	15	200.000.000	-

Sources: Ministry of Finance, OTP Research

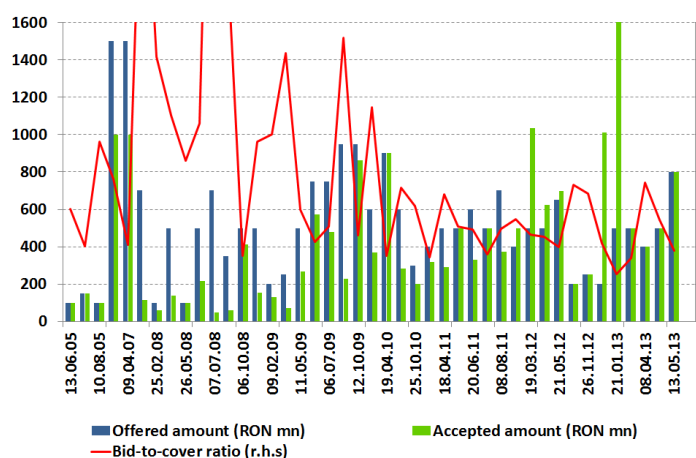
Note: * Supplementary sessions of competitive offers

6M Auctions data


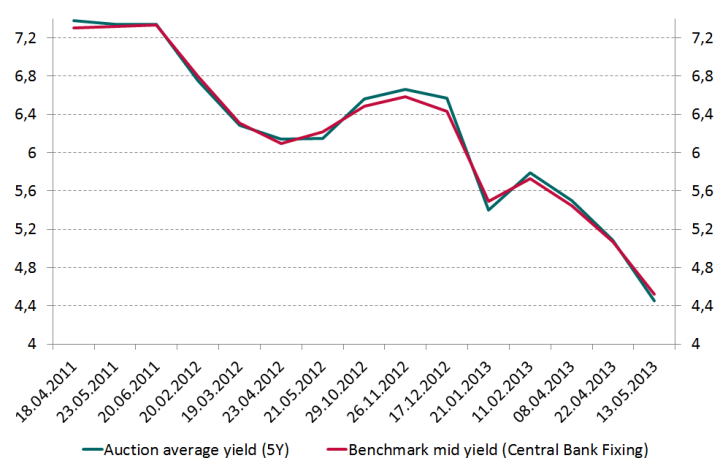
Sources: NBR, OTP Research

6M Interest rate


Sources: NBR, OTP Research

5Y Auctions data


Sources: NBR, OTP Research

5Y Interest rates


Sources: NBR, OTP Research

Last week's auction results (RON denominated)

	RO1313CTN088	RO1318DBN034
Offered amount (RON mn)	500	800
total bids (RON mn)	2981	1509
accepted amount (RON mn)	500	800
average accepted yield (%)	4,00	4,45
coupon	-	5,60

Source: NBR, OTP Research

MM: The Central Bank announced a rate cut cycle

Last week, the Central Bank kept the liquidity injection mostly unchanged. 665 mn RON went to 4 banks. This week, the amount was negligible: 107 mn RON for 2 banks. For the moment, liquidity in the money market is abundant and interest rates have fallen significantly below the base rate of 5.25%.

At the last Board meeting on monetary policy issues, the base rate was kept at 5.25% as headline inflation is still at an elevated level (5.3% YoY in April). However, the interest rate corridor around the base rate has been reduced from +/- 4 pp to +/-3 pp in order to strengthen the transmission channel of the monetary policy. The Central Bank also announced that a base rate cycle will start and this is motivated by the improved inflation outlook and backed by the evolution of both core and headline inflation this year. The core 2 inflation, the parameter which is closely followed by the Central Bank has been declining continuously this year up to 2.9% YoY in April.

Arguing that fuels inflation will be lower than previously expected and that there will also be a more favourable impact from volatile food items (fruits, vegetables, eggs) NBR lowered its inflation forecast for September and December 2013 by 0.3% to 3.2% YoY each. This places the estimated inflation within the upper limit of the targeted interval for this year (3.5% YoY). In light of new information, we expect two rate cuts this year, one in Q3 2013 and one in Q4, placing the base rate at 4.75% by the end of the year.

Last data: 10.05.2013

MID INTEREST RATES			
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)
repo rate	5,25	0	0
ROBOR ON	2,81	-181	-357
ROBOR 3M	3,86	-33	-217
ROBOR 6M	4,64	-29	-164
ROBOR 9M	4,67	-30	-161
ROBOR 1Y	4,68	-31	-163

REPO			
	Value (mn RON)	Wly chg. (mn RON)	YTD chg. (mn RON)
repo amount	665,4	-44,1	- 3.329,9

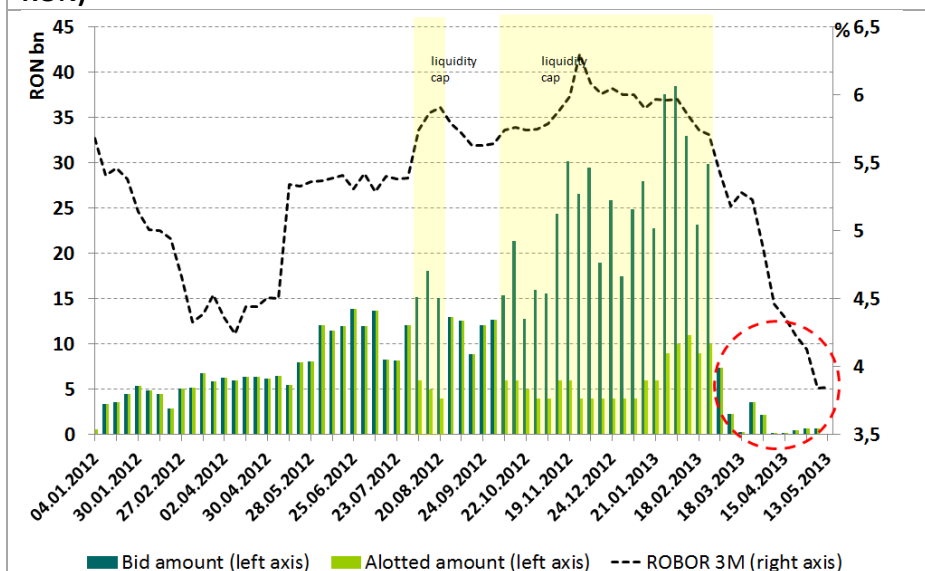
INTERBANK DEPOSITS			
	Value (mn RON)	Wly chg. (mn RON)	YTD chg. (mn RON)
outstanding	3.893,1	1103,1	991,7

MID SWAP POINTS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
USDRON 1W	13	-12	-11
USDRON 1M	86	-11	-64
USDRON 3M	275	34	29
EURRON 1W	21	-6	-19
EURRON 1M	101	-49	-44
EURRON 3M	431	-12	-79

MID EUR BASIS SWAPS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
EURRON 1Y	-85	5	70
EURRON 3Y	-73	10	83
EURRON 5Y	-73	10	78

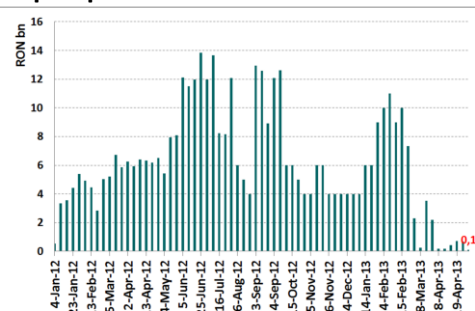
Source: Reuters

The Central Bank injected a negligible amount at this week's repo (107 mn RON)



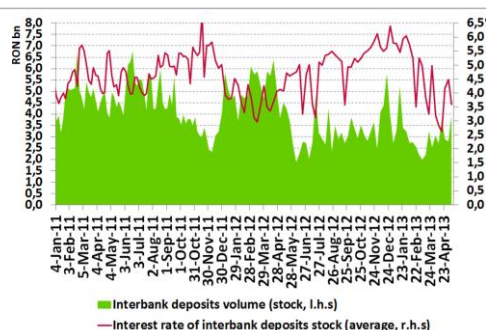
Sources: NBR, OTP Research

Repo operations since 2012



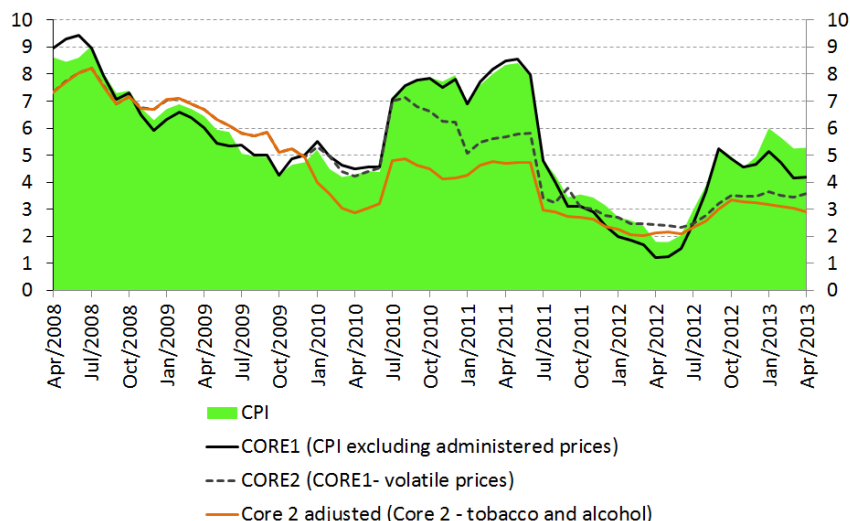
Sources: NBR, OTP Research

Interbank deposits stock and average interest rate



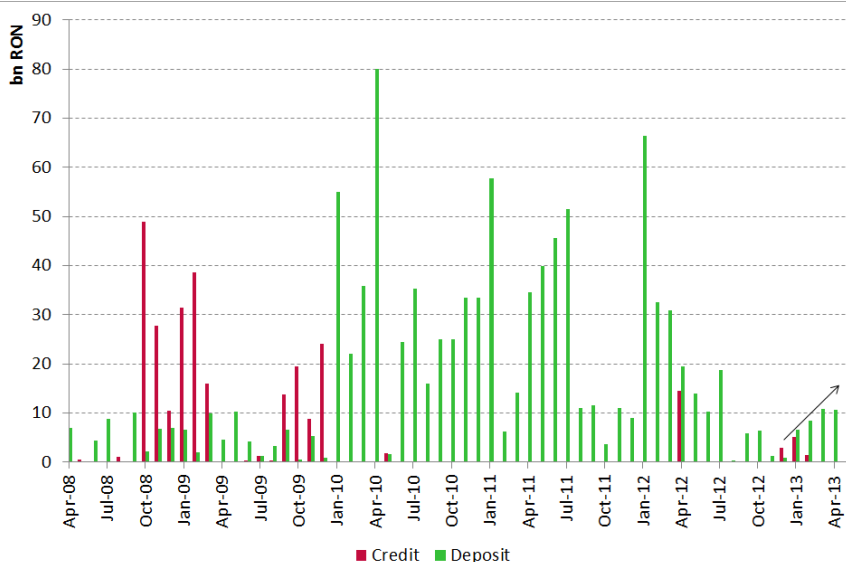
Sources: NBR, OTP Research

Core 2 adjusted continuously declined in 2013



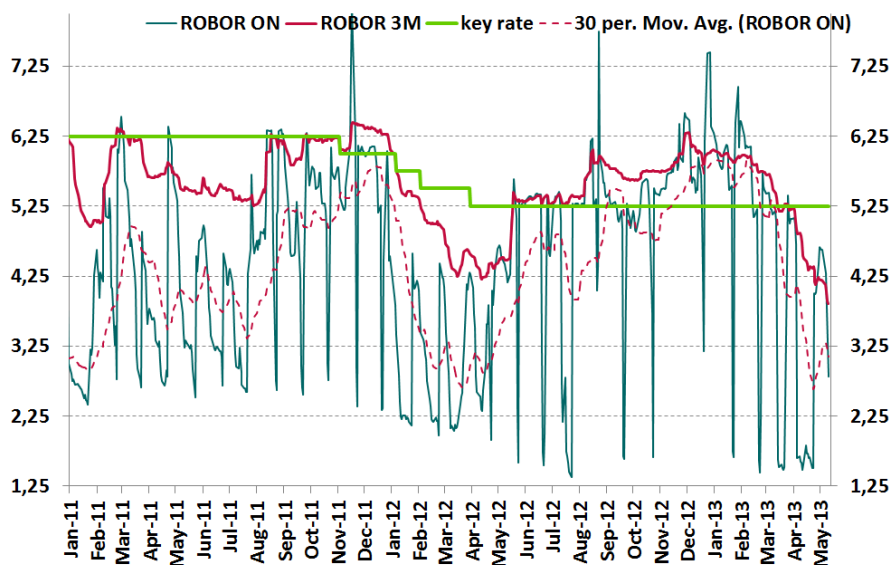
Sources: NBR, OTP Research

ON deposits with Central Bank remained unchanged in April



Sources: NBR, OTP Research

Most important MM instruments' evolution



Sources: NBR, OTP Research

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