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Weekly Report Romania

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The base rate cut cycle likely ended

Macroeconomics: Retail sales were stronger in Q4, suggesting increased consumption; industrial sales and new orders gained significant traction in December (Page 3 – 4)

Retail sales rose strongly in December (+6.7% YoY nsa and 0.6% sa), confirming that consumption was healthy. Industrial sales (+11% YoY) and new orders (+18% YoY) scored very well in December. On an annual basis, new orders data shows an improvement in Q4 (+10% YoY) as opposed to (+6% YoY) in Q3. This is in line with the positive growth outlook for the eurozone that enhances external demand. Traditionally, the bulk of FDI went to industry and as of December 2012, roughly half of the stock was in industry. Considering the improved FDI figures in 2013 we expect sector trends to be preserved and therefore we see another reason to anticipate a good evolution of industrial production in 2014. The gross wage advanced by 3.7% YoY in December and we can notice a slowdown in wage dynamics. The real wage rose by 2.1% YoY in December as inflation was at its all times low (1.6% YoY).

FX markets: The leu strengthened following NBR intervention, but MM rates are seen easing (Page 5)

The recent moves of the leu have been explained by the CB's governor on the occasion of the monetary policy decision. NBR acted on the part of the finance ministry when selling the hard currency. NBR officials suggested that we witnessed the final rate cut of the year and this sends a positive signal for the leu. Also, the chief of Treasury said that foreigners held 21% of the domestic debt (November) and that she expected no major change, basically hinting that there is no immediate threat of selloff despite the large portfolio holdings of foreigners. To this, we add that the FX reserve is comfortable and it covers the short term debt 1.7 times. While we acknowledge that NBR can defend the leu, so far the CB has allowed volatility within some limits and this is likely to continue, especially if it aims to keep interbanking rates at levels that would favor private lending. Given that MM rates are seen to fall slowly just below the base rate, we expect the leu to lose some strength from the current level.

Government securities: The Treasury cancelled this week's auctions due to yields' surge (Page 6 - 7)

The Treasury planned to sell RON 3.8 bn and EUR 200 mn in February. This plan is now challenged by the fact that it cancelled both auctions of this week, due to the surge in yields, especially at the short end where the jump has been significant: the 12M T bills yield has added more than 100 bps since the end of January, in line with the jump of money market rates. The chief of Treasury says that the funding buffer is more than 5M and that the Treasury plans to tap international market for another EUR 1 bn in H1. As MM rates are likely to see some moderate easing, we expect the yield curve to shift lower in the short term without going back to January levels.

MM: The Central Bank probably delivered the final cut of the base rate this year; required reserves eyed later on (Page 8)

The Central Bank moved on with another 25 bps rate cut to 3.5% and to our understanding, it suggested that it is the last one this year. With respect to the required reserves ratio, Mr. Isarescu said that the CB still has to analyse the effects of the cut operated in January. We expect another drop of the MRR later on this year, especially if RON lending is to be encouraged. The Central Bank revised up the inflation forecast for Q4 2014, from 3% YoY to 3.5% YoY and the main driver were the excise duties hike which was not incorporated in the previous forecast. The NBR statistics of average daily deposits placed in January at the standing facility (RON 6.6 bn) reconfirms the excess liquidity that existed in January and pushed rates significantly below the base rate. This situation was recently corrected and MM rates are now in line with the base rate. Expectations are for a mild drop in the future, below the base rate.

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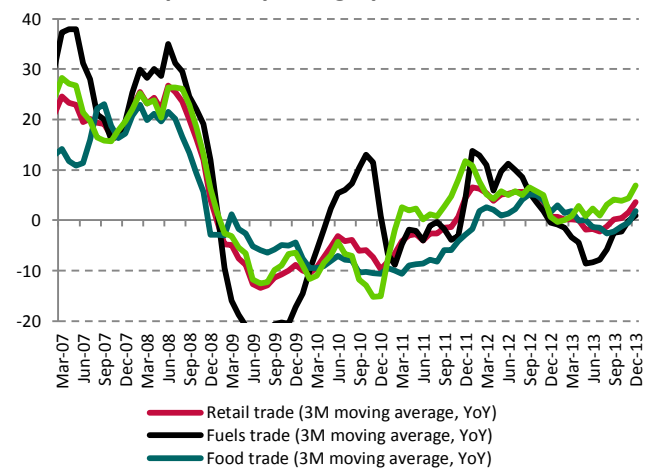
Macroeconomics: Retail sales were stronger in Q4, suggesting increased consumption; industrial sales and new orders gained significant traction in December

	PERIOD	INDICATOR	FACT	CONSENSUS	PRIOR
27 Jan	Dec	Non -governmental loans (y-o-y, %)	-3,3		-4,1
27 Jan	Dec	Non -governmental deposits (y-o-y, %)	9,3		7,0
27 Jan	Dec	M3 aggregate (y-o-y, %)	8,8		6,4
28 Jan	Dec	Bulding permits (y-o-y, %)	10,0		9,0
31 Jan	Dec	ILO unemployment (seasonally adjusted, %)	7,1		7,3
03 Feb	Dec	Retail trade turnover index (y-o-y, %)	6,7		2,1
04 Feb	Dec	Producer Price Index (y-o-y, %)	-0,1		-0,3
06 Feb	Dec	Industrial trade turnover index (y-o-y, %)	11,0		3,0
06 Feb	Dec	Index value of new orders in manufacturing (y-o-y, %)	18,0		2,4
06 Feb	Dec	Net wage growth rate (y-o-y, %)	3,7		4,8

Retail sales rose strongly in December (+6.7% YoY nsa and 0.6% sa), confirming that consumption was healthy. Q4 figures came out significantly better (+3.6% YoY) than in Q3 when sales stagnated. However just like in Q3, the strongest component was the non food sales which took off, reaching +11% YoY in December. **The retail trade sentiment is however deteriorated in January, according to the ESI indicator.**

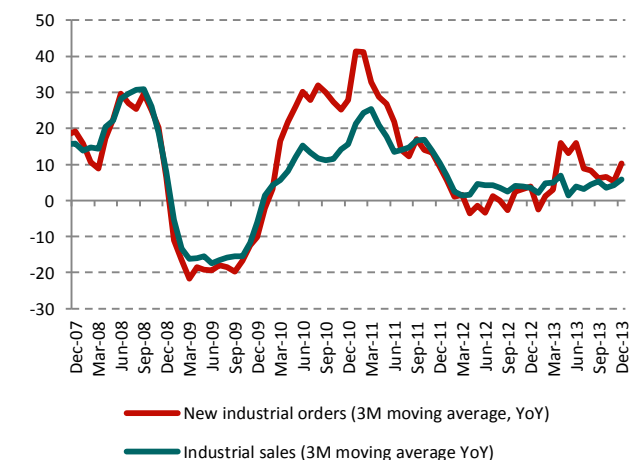
Industrial sales (+11% YoY) and new orders (+18% YoY) scored very well in December. On an annual basis, new orders data shows an improvement in Q4 (+10% YoY) as opposed to (+6% YoY) in Q3. This is in line with the positive growth outlook for the eurozone that enhances external demand. Traditionally, the bulk of FDI went to industry and as of December 2012, roughly half of the stock was in industry. 61% of the exports were from FDI enterprises activating in industry and their imports were 43% of total imports. Considering the improved FDI figures in 2013 we expect sector trends to be preserved and therefore we see another reason to anticipate a good evolution of industrial production in 2014. **For January though, the ESI industrial sentiment shows a deterioration compared to December.**

Retail sales rose by 6.7% YoY in December, showing that consumption is picking up



Source: NIS, OTP Research

New orders and industrial sales were strong in December

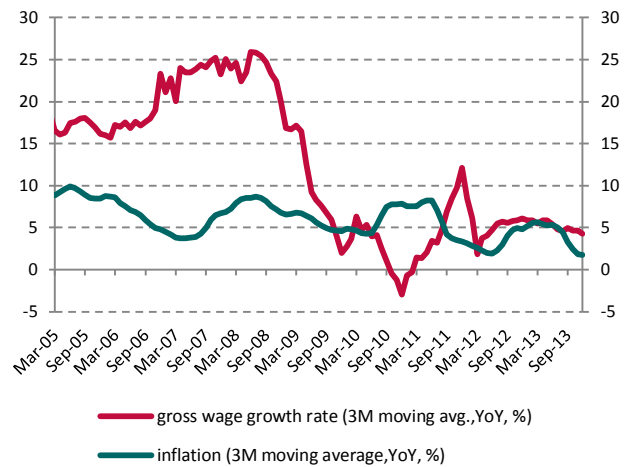


Source: NIS, OTP Research

The gross wage advanced by 3.7% YoY in December and we can notice a slowdown in wage dynamics. The real wage rose by 2.1% YoY in December as inflation was at its all times low (1.6% YoY).

Producer prices' decline almost stopped in December (-0.1% YoY) as opposed to (-0.3% YoY) in November as the foreign prices component slowed down their fall. In December, external market prices fell by 2.2% YoY compared to 2.7%YoY in November, which is partly explained by the leu's appreciation in the same period: it gained 0.6% YoY on average to the euro in December 2013.

Gross wages' hike slows down, but real wage is Up by 2.1% YoY



Source: NIS, OTP Research

Medium-term macroeconomic forecast

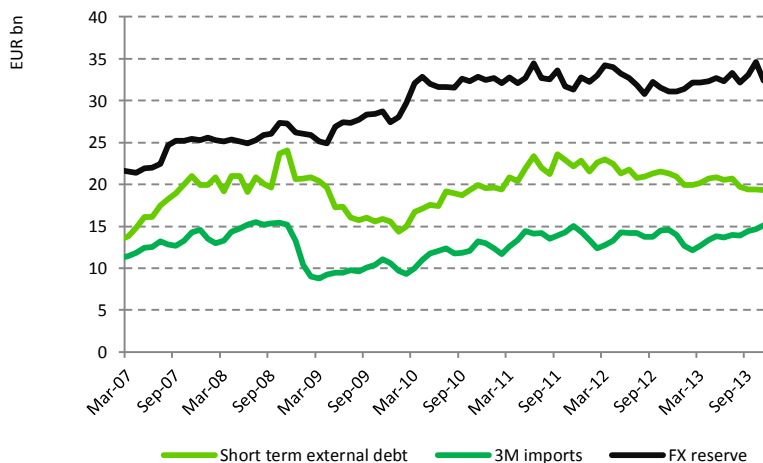
Main macroeconomic indicators	Fact						Forecast	
	2007	2008	2009	2010	2011	2012	2013	2014
Real GDP	6,3%	7,3%	-6,6%	-1,1%	2,2%	0,7%	2,5%	2,0%
Actual individual consumption of households								
Households consumption expenditure	12,0%	9,0%	-10,4%	-0,2%	1,2%	1,0%	0,7%	2,3%
Government consumption	2,5%	6,2%	9,5%	-13,7%	-0,3%	2,4%	-1,3%	1,4%
Gross fixed capital formation	30,3%	15,6%	-28,1%	-1,8%	7,3%	4,9%	-4,0%	4,5%
Exports	7,8%	8,3%	-6,4%	13,2%	10,3%	-3,0%	5,4%	5,9%
Imports	27,3%	7,9%	-20,5%	11,1%	10,0%	-0,9%	1,4%	6,9%
Consumer prices (avg.)	4,8%	7,8%	5,6%	6,1%	5,8%	3,3%	4,1%	2,4%
Budget Balance (GDP%, ESA 95)	-2,9%	-5,7%	-9,0%	-6,8%	-5,6%	-3,0%	-2,9%	-2,8%
Public debt (GDP %)	12,8%	13,4%	23,6%	30,5%	34,7%	37,9%	38,5%	39,1%
CA balance (% GDP)	-13,4%	-11,6%	-4,2%	-4,4%	-4,5%	-4,4%	-0,6%	-2,8%
CA balance (bn EUR)	-16,8	-16,2	-4,9	-5,5	-5,9	-5,8	-0,9	-4,2
Unemployment	6,4%	5,8%	6,9%	7,3%	7,4%	7,0%	7,5%	7,5%
Nominal wage growth	21,8%	26,1%	4,8%	3,1%	4,1%	4,6%	5,0%	4,9%
Real wage growth	14,7%	16,5%	-1,5%	-3,7%	-1,9%	1,2%	0,9%	2,4%
Key interest rate (avg.)	7,5%	9,7%	9,1%	6,5%	6,2%	5,33%	4,79%	3,52%
Key interest rate (e.o.p.)	7,5%	10,3%	8,0%	6,3%	6,0%	5,25%	4,00%	3,50%
EUR/RON (avg.)	3,34	3,68	4,24	4,21	4,24	4,46	4,42	4,46
EUR/RON (e.o.p.)	3,61	3,99	4,23	4,28	4,32	4,43	4,47	4,44

Source: Eurostat, NBR, OTP Research

FX markets: The leu strengthened following NBR intervention, but MM rates are seen easing

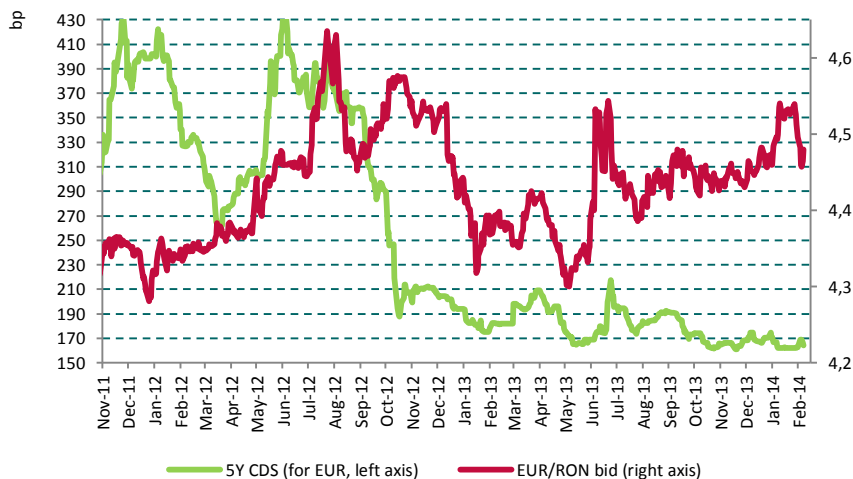
The recent moves of the leu have been explained by the Central Bank's governor on the occasion of the monetary policy decision. The governor explained that NBR acted on the part of the finance ministry when selling the hard currency as the Treasury proceeded to make payments. The fact that **NBR officials suggested that we have witnessed the last base rate cut of the year sends a positive signal for the leu.** Also, the chief of Treasury Diana Popescu said that foreigners held 21% of the domestic debt and that she expected no major change, basically hinting that there is no immediate threat of selloff despite the large portfolio holdings of foreigners. To this, we add that **the FX reserve is comfortable and it covers the short term 1.7 times.** While we acknowledge that NBR can defend the leu, so far the Central Bank has allowed volatility within some limits and it is likely to continue, especially if it aims to keep interbanking rates at levels that would favor private lending. **Given that money market rates are seen to fall slowly, just below the base rate, we expect the leu to lose some strenght from the current level.**

The FX reserve covers comfortably the short term external debt



Sources: NBR, NIS

Following NBR's intervention, the leu strengthened



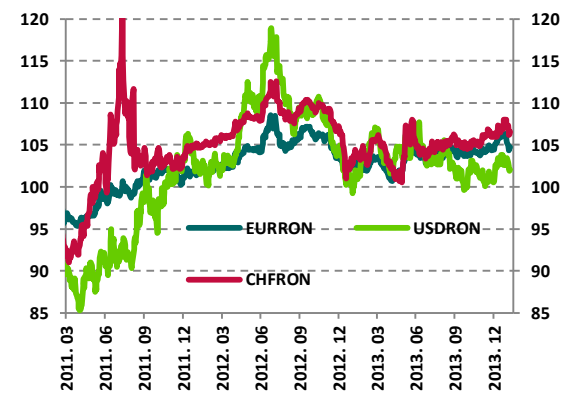
Sources: Reuters

Last data: 06.02.2014

FX BID				
	Value		Weekly chg. (%)	YTD chg. (%)
EURRON	4,47	↓	-1,06	↑ 0,11
USDRON	3,29	↓	-1,31	↑ 1,30
CHFRON	3,65	↓	-1,13	↑ 0,08
RONJPY	3,22	↓	-0,71	↑ 4,48
RONPLN	1,07	↑	0,30	↓ -0,31
100HUFRON	1,45	↓	-0,22	↓ -2,99
RONCZK	0,16	↓	-0,67	↓ -0,37
RONRUB	0,09	↓	-0,75	↓ -4,08
RONRSD	0,04	↓	-1,31	↓ -1,21
RONBGN	2,28	↓	-1,04	↑ 0,17

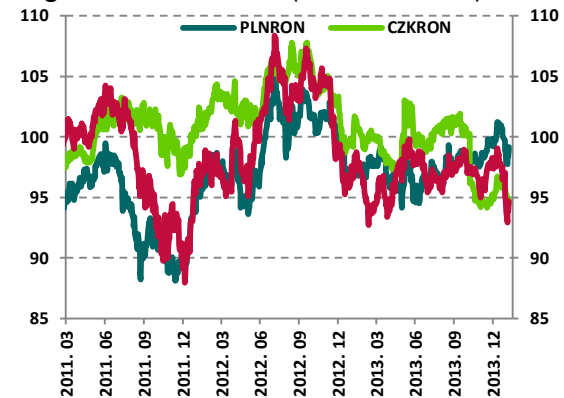
Source: Reuters

Major RON FX rates (03.01.2011=100)



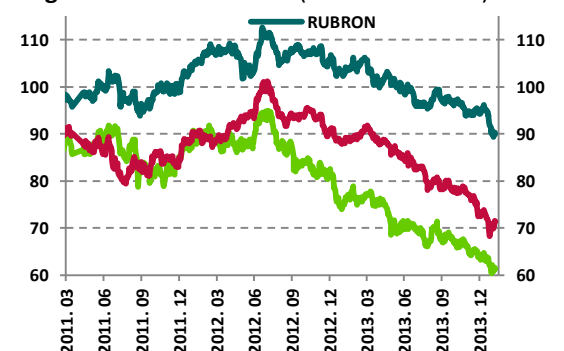
Sources: Reuters

Regional RON FX rates I. (03.01.2011=100)



Sources: Reuters

Regional RON FX rates II. (03.01.2011=100)



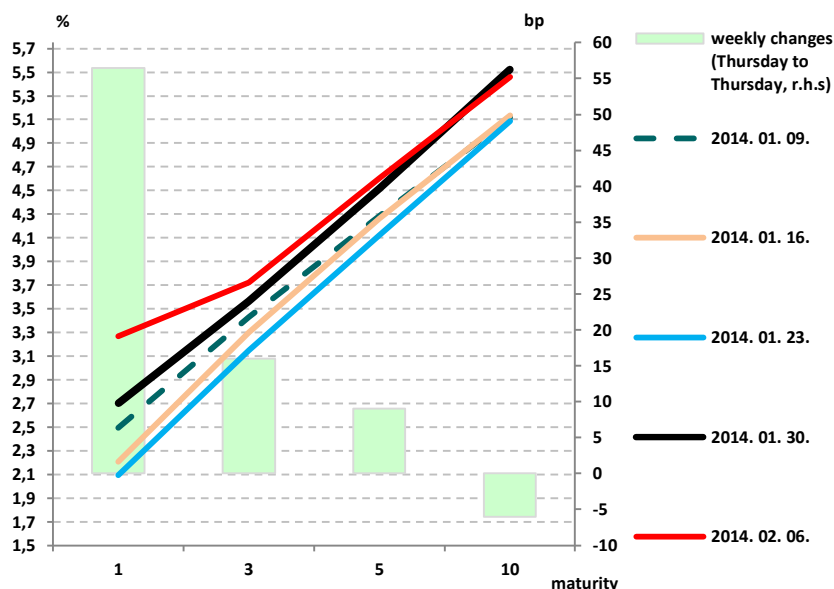
Sources: Reuters

Government securities: The Treasury cancelled this week's auctions due to yields' surge

The Treasury planned to sell RON 3.8 bn and EUR 200 mn in February, mostly in bonds with an average residual maturity of 5-7 years, as it tries to prolonge the average maturity of government debt. This plan is now challenged by the fact that the Treasury cancelled both auctions of this week, due to the surge in yields, especially at the short end where the jump has been significant: **the 12M T bills yield has added more than 100 bps since the end of January**, in line with the jump of money market rates. Part of this week's sales was RON 1.2 bn in 12M T-bills. The chief of Treasury says that the funding buffer is more than 5M and that the Treasury plans to tap international market for another EUR 1 bn in H1.

As money market rates are likely to see some moderate easing, we expect the yield curve to shift lower in the short term without going back to January levels.

Yield curve over the past weeks (Central Bank fixing)



Source: NBR, OTP Research

T - bills auctions in February (in RON)

ISIN	Auction date	Settlement date	Maturity	Months	Indicative target amount (RON)
RO1415CTN032	03.02.2014	05.02.2014	04.02.2015	12	1.200.000.000

Sources: Ministry of Finance

Bond auctions in February (in RON)

ISIN	Auction date	SSON auction date	Settlement date	Maturity	Years	Residual Maturity	Indicative target amount (RON)	Indicative target amount SSON* (RON)
RO1121DBN032	06.02.2014	07.02.2014	10.02.2014	11.06.2021	10,0	7,37	600.000.000	60.000.000
RO0717DBN038	10.02.2014	11.02.2014	12.02.2014	11.06.2017	10,0	3,37	800.000.000	80.000.000
RO1323DBN018	13.02.2014	14.02.2014	17.02.2014	26.04.2023	10,0	9,25	100.000.000	10.000.000
RO1116DBN024	17.02.2014	18.02.2014	19.02.2014	30.04.2016	5,0	2,25	500.000.000	50.000.000
RO1419DBN014	24.02.2014	25.02.2014	26.02.2014	24.06.2019	5,0	5,4	600.000.000	60.000.000

Sources: Ministry of Finance

Note: * Supplementary sessions of competitive offers

Bond auctions in February (in EUR)

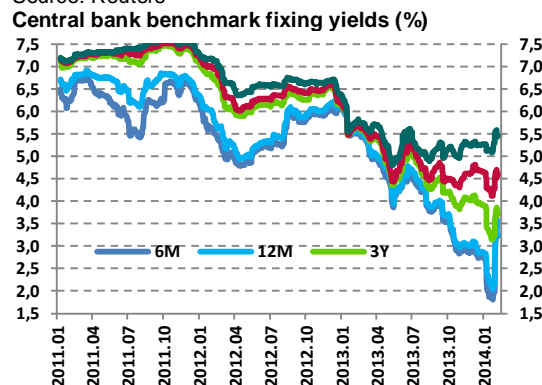
ISIN	Auction date	Settlement date	Maturity	Months	Coupon	Indicative target amount (EUR)
RO1419DBE013	20.02.2014	24.02.2014	21.01.2019	5	3,4	200.000.000

Sources: Ministry of Finance

Last data: 06.02.2014

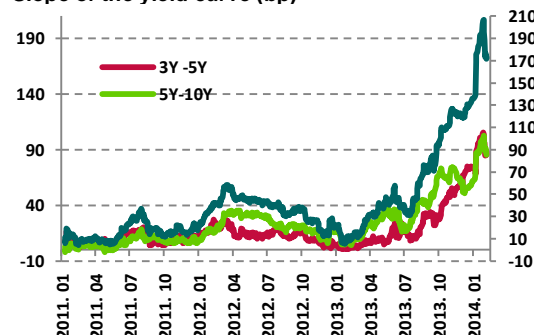
RON GOVERNMENT SECURITIES				
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)	
6M	3,24	↑ 66	↑ 49	
12M	3,27	↑ 57	↑ 41	
3Y	3,72	↑ 16	↓ -19	
5Y	4,61	↑ 9	↓ -4	
10Y	5,46	↓ -6	↑ 19	
SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
GERROM 3Y	354	↑ 16	↑ 1	
GERROM 5Y	390	↑ 9	↑ 19	
GERROM 10Y	380	↓ -6	↑ 47	
3Y-5Y	89	↓ -7	↑ 15	
5Y-10Y	86	↓ -15	↑ 24	
3Y-10Y	174	↓ -22	↑ 38	
FLY 3-5-10	-3	↓ -8	↑ 9	
CDS MID SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
3Y EURO	113	↑ 4	↓ -4	
5Y EURO	166	↑ 4	↓ -4	

Source: Reuters



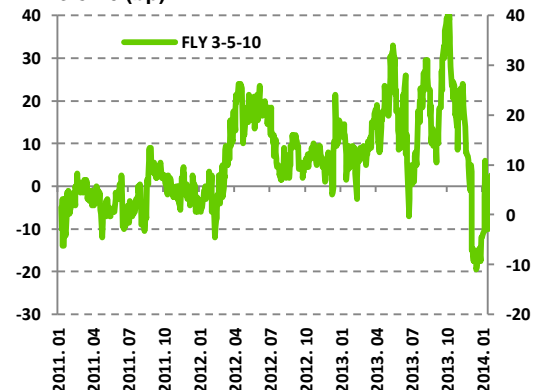
Sources: NBR

Slope of the yield curve (bp)



Sources: NBR

FLY 3-5-10 (bp)

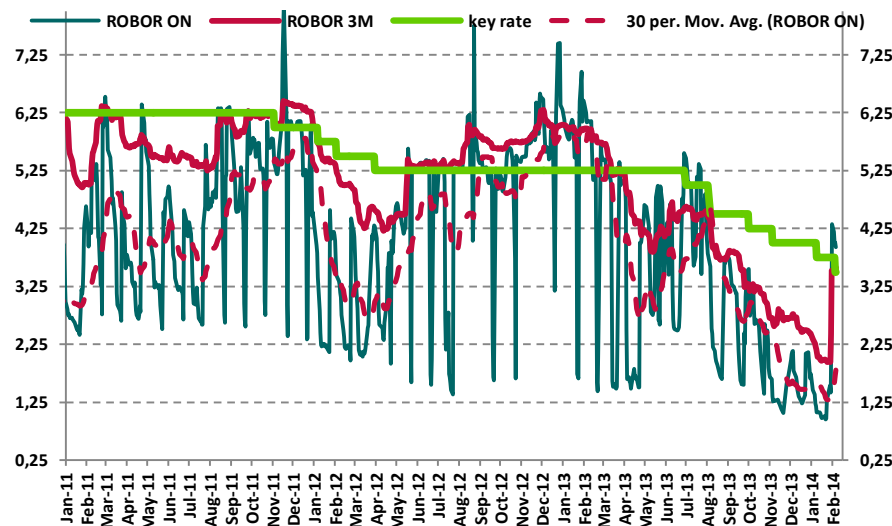


Sources: NBR

MM: The Central Bank probably delivered the final cut of the base rate this year; required reserves eyed later on

The Central Bank moved on with another 25 bps rate cut to 3.5% and to our understanding, it suggested that it is the last one this year. Also, the governor stated that the current levels of the money market rates are in line with the base rate. Regarding the future, a slow easing is expected, just below the base rate. Although on average this could be the case, throughout the year we could see some more volatility, driven by the combination of internal and external events at the horizon and considering the wide variation band around the base rate +/- 300 bps. With respect to the required reserves ratio, Mr. Isarescu said that the CB still has to analyse the effects of the cut operated in January. **We expect another drop of the MRR later on this year, especially if RON lending is to be encouraged.**

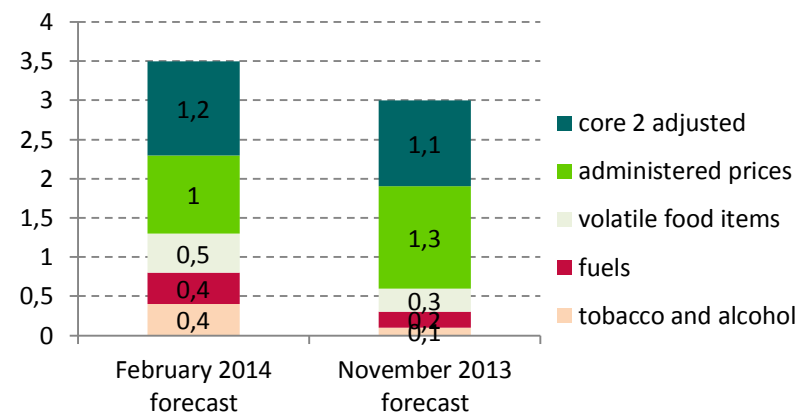
Most important MM instruments' evolution



Sources: NBR, OTP Research

The Central Bank revised up the inflation forecast for Q4 2014, from 3% YoY to 3.5% YoY and the main driver were the excise duties hike which was not incorporated in the previous report and was mentioned to the risks of the forecast. Thereby, main items affected were fuels, tobacco and alcohol's contributions to CPI (please see table below). The volatile

NBR raised December 2014 inflation forecast by 0.5 pp to 3.5%



Sources: NBR, OTP Research

Last data: 06.02.2014

MID INTEREST RATES			
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)
repo rate	3,50	0	-50
ROBOR ON	3,93	148	184
ROBOR 3M	3,57	114	107
ROBOR 6M	3,41	68	41
ROBOR 9M	3,39	54	24
ROBOR 1Y	3,39	47	20

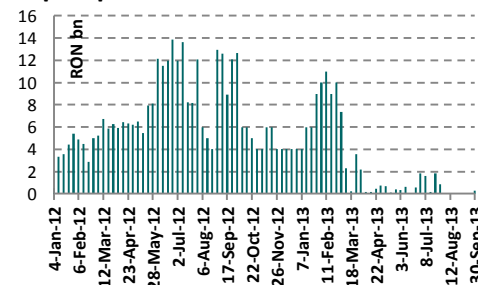
INTERBANK DEPOSITS			
	Value (mn RON)	Wly chg. (mn RON)	YTD chg. (mn RON)
outstanding	5.103,6	-753,1	464,4

MID SWAP POINTS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
USDRON 1W	23	4	14
USDRON 1M	84	26	50
USDRON 3M	208	-31	90
EURRON 1W	31	10	21
EURRON 1M	111	31	67
EURRON 3M	338	129	161

MID EUR BASIS SWAPS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
EURRON 1Y	-80	0	0
EURRON 3Y	-70	0	0
EURRON 5Y	-70	0	0

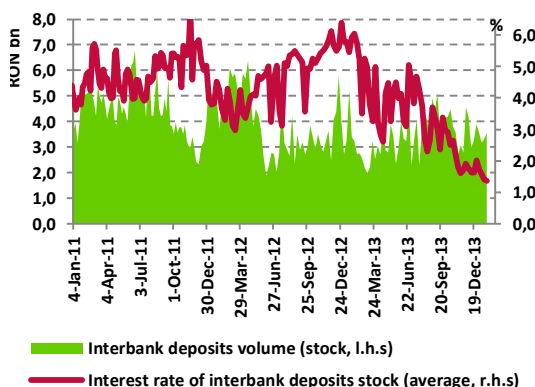
Source: Reuters

Repo operations since 2012



Sources: NBR, OTP Research

Interbank deposits stock and average interest rate

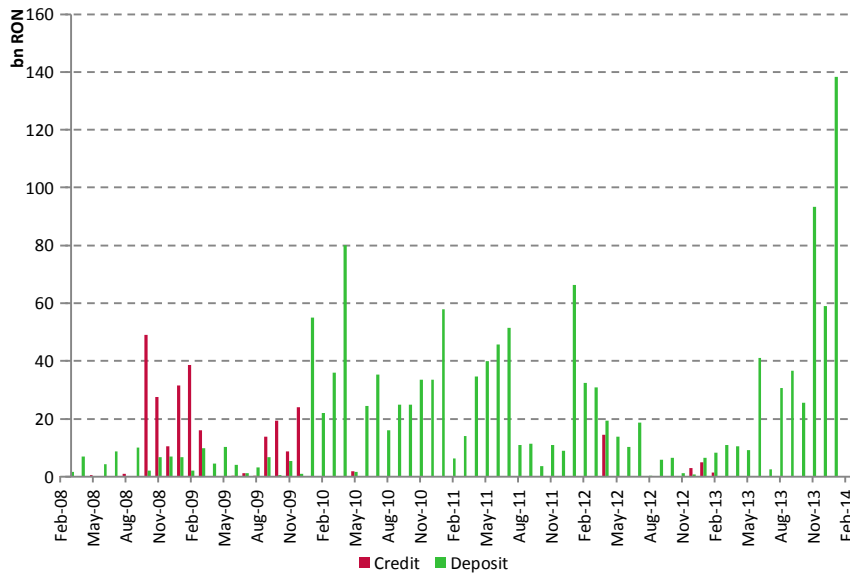


Sources: NBR, OTP Research

foods' contribution was also revised upwards.

The NBR statistics of average daily deposits placed in January at the standing facility (RON 6.6 bn) reconfirms the excess liquidity that existed in January and pushed rates significantly below the base rate. This situation was recently corrected and MM rates are now in line with the base rate.

ON deposits to the NBR's facility skyrocketed in January, with the daily amount averaging RON 6.6 bn compared to RON 3 bn in December



Sources: NBR, OTP Research

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