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Weekly Report

Romania

28 July 2014

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Eyes on the budget

Macroeconomics: private lending down 4% YoY in June (Page 3- 4)

Banking statistics data for June did not bring any surprises. Private lending continued to drop (-3.9% YoY), led by the corporate sector (-5%) which is repaying FX debt without contracting new loans. Also, based on the maturity profile, not only the investment loans are suffering, but the working capital loans are declining as well (-12.5% YoY). The housing sector goes forward with investment decisions as the mortgage loans added 7% YoY. The mortgage RON component nearly tripled due to the FX restrictions but it has still large room to increase: it represents only 14% of the stock. Consumer loans continue to contract (-8.3% YoY). Private deposits added 5.9% YoY, with the corporate sector leading the way (+9.4% YoY). RON deposits remain the favorite ones (+8.5% YoY) due to the higher interest rates but the foreign currency deposits are also making progress (+3% YoY, in euro equivalent).

FX market: fiscal risks on the horizon (Page 5 - 6)

The EUR/RON pair fell back below 4.40 level, after news related to the inclusion of another domestic ISIN in the JP-Morgan Index broke out. The depreciation of euro was broader as leu's peers benefited as well while the euro sank to its yearly low against the dollar. The moment bears more importance due to a change in nuance of Janet Yellen confessing to the US Congress: she stated that the FOMC could hike rates faster than expected (currently in mid year 2015) provided the labour market outpaces Fed's expectations. As the market consensus will fully adopt this view, depreciation pressures are likely to be felt. Additionally, we continue to reiterate the risks associated with a lax fiscal policy, especially in an electoral year. The dynamics of revenues and expenditures keep deteriorating. In H1 2014, the cash budget deficit stood at 0.5%. The 12M rolling figures point to a budget deficit of 1.9% so far versus the planned 2.2%. However, it does not take into account a significant change in taxes, such as the CAS.

Fixed income markets: new ISIN in JP Morgan Index (Page 7 - 8)

The yield curve dropped lower last week, especially at the long end, where the 5Y and 10Y bond yields shed off 10 and 17 bps respectively. This move took place for maturity horizons not perceived as completely exhausted considering the potential real yield gains. The Treasury sold bonds at still declining yields by 22-25 bps. The market reaction was boosted by the news that JP Morgan included a new domestic ISIN in its emerging market bond index and it also included the Romanian securities in another index GBI-EM Global Diversified Investment Grade Index. 70% of RON outstanding government securities mature between 2014-2017 but in this maturity range, prices have already reached their highs.

Money markets: summer ease (Page 9)

Liquidity conditions are at good levels and no pressure was felt last week, when corporate quarterly payments were due. The high government debt redemptions of July will help liquidity conditions in August as well, especially since the month has been slower from the auctions point of view in the past few years. With inflation rate posing little pressure in Romania and in the region as well, it is possible that the Central Bank will take further steps to ease the monetary policy as money market rates are persistently below the base rate. However the move should be carefully planned as the last quarter promises to be eventful due to domestic and external factors as well.

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Macroeconomics: private lending down 4% YoY in June

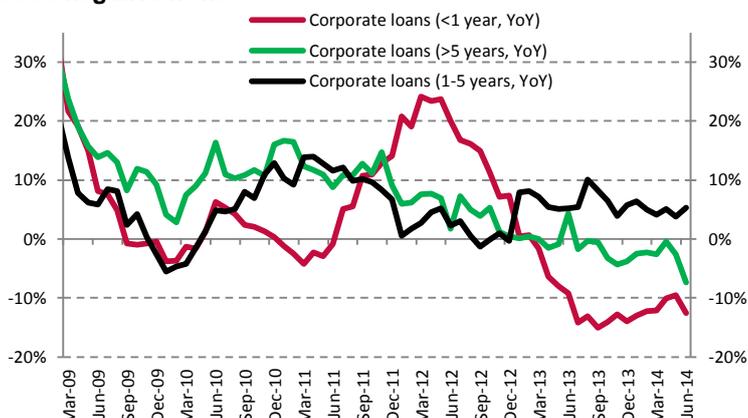
	PERIOD	INDICATOR	FACT	CONSENSUS	PRIOR
23 Jul	June	Non-governmental loans (y-o-y, %)	-3.9		-2.1
23 Jul	June	Non-governmental deposits (y-o-y, %)	5.9		6.6
23 Jul	June	M3 aggregate (y-o-y, %)	5.3		6.5
29 Jul	June	Bulding permits (y-o-y, %)			6.6
31 Jul	June	ILO unemployment (seasonally adjusted, %)			7.3

Banking statistics data for June did not bring any surprises.

Private lending continued to drop (-3.9% YoY), led by the corporate sector (-5%) which is repaying FX debt without contracting new loans. Also, based on the maturity profile, not only the investment loans are suffering, but the working capital loans are declining as well (-12.5% YoY). The housing sector goes forward with investment decisions as the mortgage loans added 7% YoY. The mortgage RON component nearly tripled due to the FX restrictions but it has still large room to increase: it represents only 14% of the stock. Consumer loans continue to contract (-8.3% YoY).

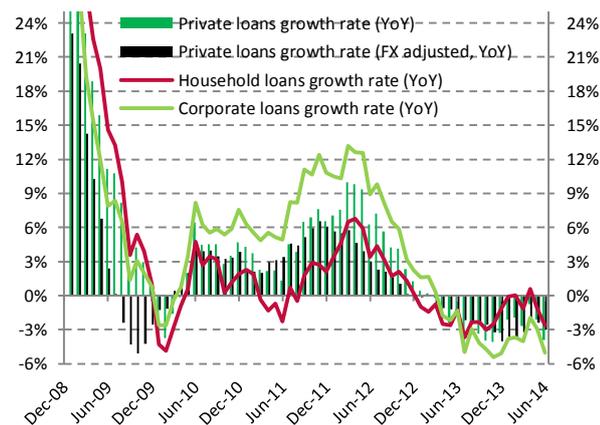
Private deposits added 5.9% YoY, with the corporate sector leading the way (+9.4% YoY). RON deposits remain the favorite ones (+8.5% YoY) due to the higher interest rates but the foreign currency deposits are also making progress (+3% YoY, in euro equivalent).

Short term corporate loans fall rapidly (-12.5% YoY); long term loans also see negative flows



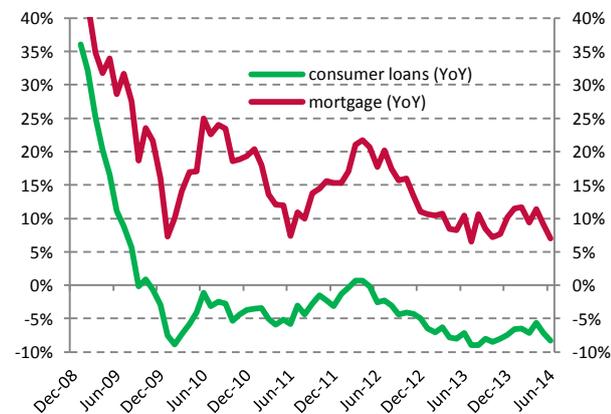
Source: NBR

Private lending headed lower in June (-3.9% YoY) led by the corporate component



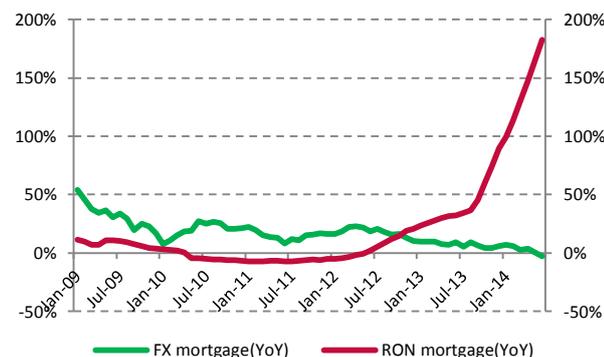
Source: NBR

Consumer loans are still far from heading up

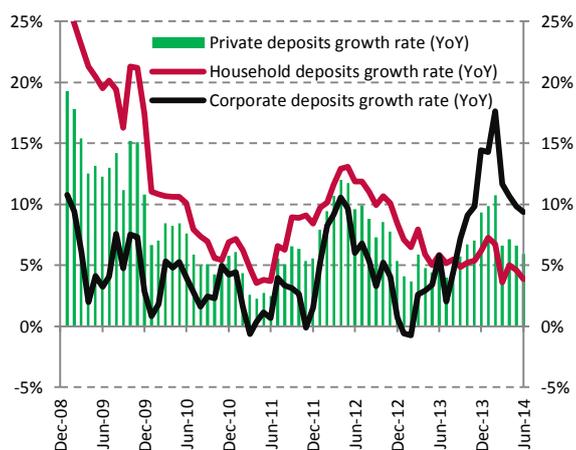


Source: NBR

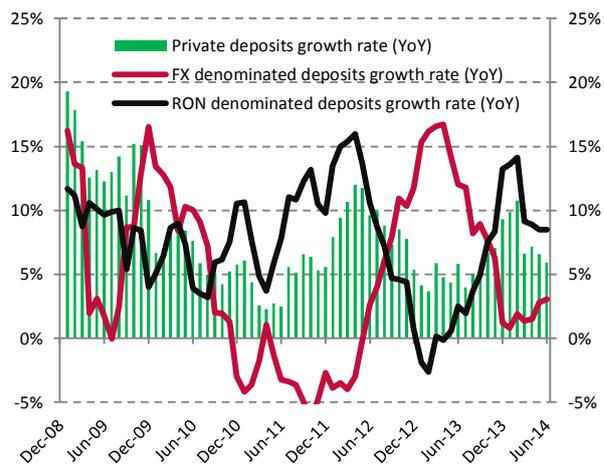
RON denominated mortgage loans nearly tripled in a year, as of June (YoY)



Source: NBR

Corporate deposits increase the fastest (+9.4%YoY)


Source: NBR

Due to higher interest rates, RON deposits are preferred


Source: NBR

Macroeconomic forecast

Main macroeconomic indicators			Fact					Forecast	
	2007	2008	2009	2010	2011	2012	2013	2014	2015
Nominal GDP (EUR mn)	124,729	139,765	118,196	124,328	131,327	131,747	142,395	147,487	156,675
Real GDP	6.3%	7.3%	-6.6%	-1.1%	2.3%	0.6%	3.5%	3.0%	3.0%
Households consumption expenditure	12.0%	9.0%	-10.4%	-0.2%	1.6%	1.1%	1.3%	2.2%	2.9%
Government consumption	2.5%	6.2%	9.5%	-13.7%	-3.0%	0.7%	-1.7%	2.9%	2.7%
Gross fixed capital formation	30.3%	15.6%	-28.1%	-1.8%	7.7%	3.8%	-3.3%	2.2%	6.8%
Exports	7.8%	8.3%	-6.4%	13.2%	11.6%	-1.5%	13.5%	9.4%	6.6%
Imports	27.3%	7.9%	-20.5%	11.1%	10.5%	-0.2%	2.4%	8.3%	6.5%
Consumer prices (avg.)	4.8%	7.8%	5.6%	6.1%	5.8%	3.3%	4.0%	2.2%	2.9%
Budget Balance (GDP%, ESA 95)	-2.9%	-5.7%	-9.0%	-6.8%	-5.5%	-3.0%	-2.3%	-2.8%	-2.5%
Public debt (GDP %)	12.8%	13.4%	23.6%	30.5%	34.7%	38.0%	38.4%	39.4%	39.8%
CA balance (% GDP)	-13.4%	-11.6%	-4.2%	-4.4%	-4.5%	-4.4%	-1.1%	-2.0%	-2.0%
CA balance (bn EUR)	-16.8	-16.2	-4.9	-5.5	-5.9	-5.8	-1.5	-2.9	-3.1
Unemployment	6.4%	5.8%	6.9%	7.3%	7.4%	7.0%	7.3%	7.0%	6.8%
Nominal wage growth	21.8%	26.1%	4.8%	3.1%	4.1%	4.6%	5.0%	4.6%	5.4%
Real wage growth	14.7%	16.5%	-1.5%	-3.7%	-1.9%	1.2%	1.0%	2.4%	2.4%
Key interest rate (avg.)	7.5%	9.7%	9.1%	6.5%	6.2%	5.3%	4.8%	3.5%	3.5%
Key interest rate (e.o.p.)	7.5%	10.3%	8.0%	6.3%	6.0%	5.3%	4.0%	3.5%	3.5%
EUR/RON (avg.)	3.34	3.68	4.24	4.21	4.24	4.46	4.41	4.48	4.45
EUR/RON (e.o.p.)	3.61	3.99	4.23	4.28	4.32	4.43	4.46	4.44	4.45

	1Q 2013	2Q 2013	3Q 2013	4Q 2013	1Q 2014	2Q 2014	3Q 2014 F	4Q 2014 F	1Q 2015 F
EUR/RON (end of period)	4.39	4.48	4.46	4.46	4.46	4.39	4.41	4.44	4.43
Central Bank Rate (%)	5.25	5.25	4.50	4.00	3.5	3.5	3.5	3.5	3.5
3-Month Robor (%)	5.35	4.45	3.65	2.58	2.97	2.42	3.02	3.21	3.31
Ten-Year Bond (% mid yield, NBR fixing)	5.64	5.45	5.16	5.28	5.27	4.40	4.75	5.05	5.35

Source: Eurostat, NIS, NBR, OTP Research

FX markets: fiscal risks on the horizon

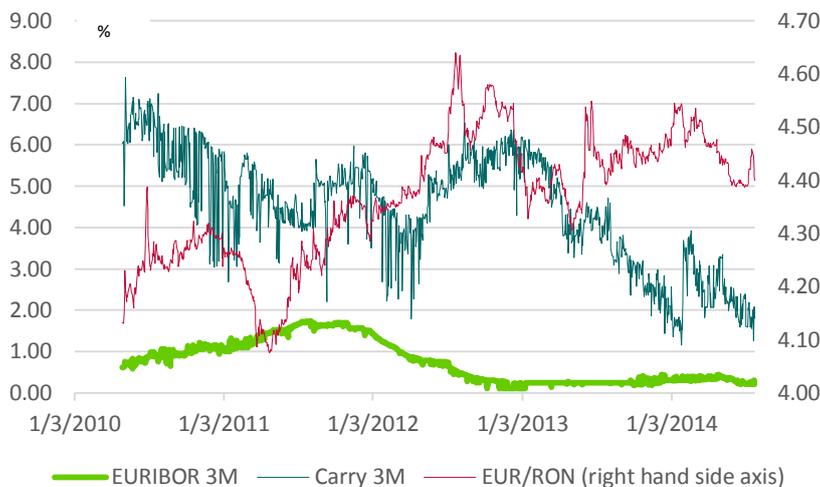
The EUR/RON pair fell back below 4.40 level, after the news related to the inclusion of another domestic ISIN in the JP-Morgan Index. The depreciation of euro was broader as leu's peers benefited as well while the euro sank to its yearly low against the dollar. The moment bears more importance due to a change in nuance of Janet Yellen confessing to the US Congress: she stated that the FOMC could hike rates faster than expected (currently in mid year 2015) provided the labour market outpaces Fed's expectations. As the market consensus will fully adopt this view, depreciation pressures are likely to be felt.

Date: 25.07.2014

FX BID				
	Value		Weekly chg. (%)	YTD chg. (%)
EURRON	4.39	↓	-1.44	↓ -1.17
USDRON	3.27	↓	-0.69	↓ -2.83
CHFRON	3.61	↓	-1.39	↓ -1.70
RONJPY	3.21	↓	-1.18	↓ -17.21
RONPLN	1.06	↓	-1.27	↓ -2.56
100HUFRON	1.42	↓	-1.07	↓ -6.69
RONCZK	0.16	↓	-1.60	↓ -9.72
RONRUB	0.09	↓	-0.61	↓ -15.51
RONRSD	0.04	↓	-1.64	↓ -4.70
RONBGN	2.25	↓	-1.39	↓ -1.10

Source: Reuters

The leu strenghtened temporarily



Source: Reuters

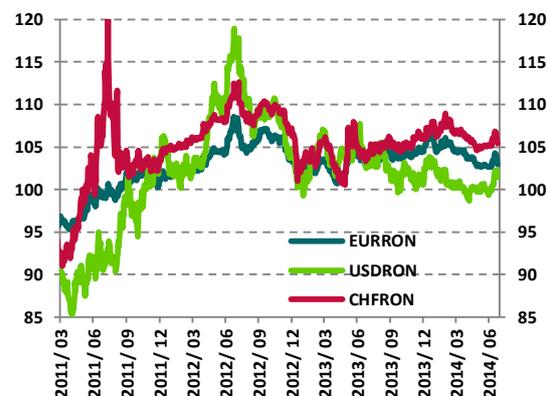
Daily EUR/RON Chart



Source: Reuters

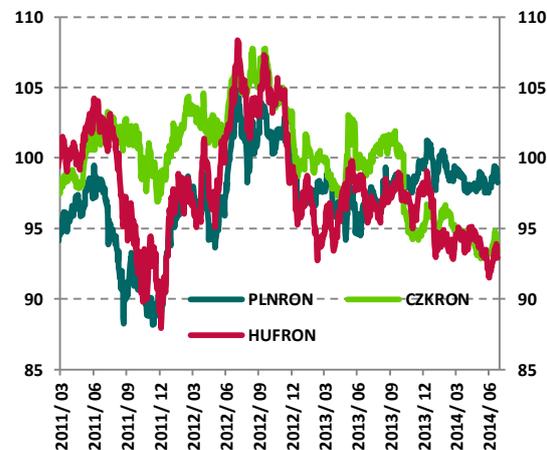
Major trend:	↓
Minor trend:	↓
R1: 4.4050	S1: 4.39
R2: 4.41	S2: 4.38
R3: 4.42	S3: 4.3670
RSI: neutral	

Major RON FX rates (03.01.2011=100)



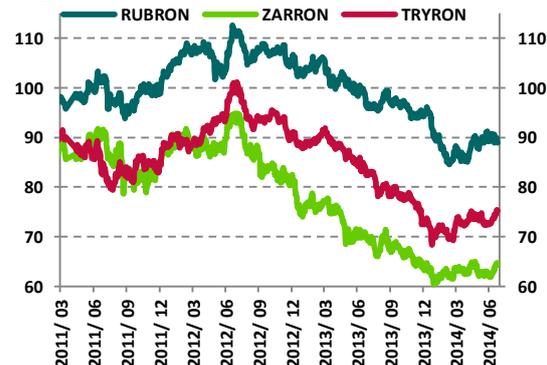
Sources: Reuters

Regional RON FX rates (03.01.2011=100)



Sources: Reuters

Regional RON FX rates (03.01.2011=100)



Sources: Reuters

Additionally, we continue to reiterate **the risks associated with a lax fiscal policy**, especially in an electoral year. The dynamics of revenues and expenditures keep deteriorating (please see table below). **In H1 2014, the cash budget deficit stood at 0.5%**. Current revenues advanced by 2.8% YoY in June compared to 3.7% YoY in May. Current expenditures rose by 2.3% YoY versus 0.7% YoY in May. The 12M rolling figures point to a budget deficit of 1.9% so far versus the planned 2.2%. However, it does not take into account a significant change in taxes, such as the CAS.

The cash budget deficit evolution up to June 2014

	2014 budget	June-14 (cumulated)	12M rolling	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Apr-14	May-14	Jun-14
	RON mn	RON mn	RON mn	YoY	YoY	YoY	YoY	YoY	YoY	YoY	YoY
Total revenue	215,958	100,384	202,885	3.0%	4.9%	4.4%	3.6%	3.8%	4.4%	3.7%	2.9%
Current income	200,481	97,100	193,251	4.8%	5.3%	4.8%	3.6%	3.3%	4.4%	3.7%	2.8%
Fiscal income	125,312	60,888	121,289	6.0%	6.8%	6.2%	4.4%	5.0%	7.0%	7.0%	3.7%
Income tax	36,725	18,192	35,854	3.0%	4.2%	5.2%	6.5%	1.8%	4.9%	4.5%	5.4%
Corporate income tax	12,710	6,099	11,615	-10.2%	-5.5%	-1.3%	0.7%	8.1%	12.9%	11.3%	12.7%
Personal income tax	24,001	11,421	22,806	11.5%	9.3%	7.9%	8.5%	-3.5%	-2.1%	-1.0%	0.6%
Other tax on income, profit and capital	14	672	1,433	-4.8%	9.5%	21.3%	30.2%	58.4%	41.8%	43.4%	33.3%
Property tax	5,041	3,695	5,361	4.8%	9.5%	9.7%	8.4%	13.3%	7.3%	34.7%	35.0%
Taxes on goods and services	82,513	38,480	79,077	7.7%	8.0%	6.7%	3.5%	5.8%	8.3%	6.0%	0.8%
Value added tax	53,772	24,675	52,286	9.5%	2.3%	4.1%	2.6%	-0.5%	2.7%	1.4%	1.9%
Excise duties	24,102	11,056	22,193	9.3%	4.2%	2.8%	4.2%	14.0%	15.2%	9.8%	10.9%
Other	4,639	2,749	4,598	-14.4%	87.5%	55.8%	9.2%	43.6%	43.4%	43.5%	-31.2%
Taxes on international commerce	623	313	620	2.8%	-5.2%	-16.3%	-12.3%	-2.1%	0.4%	0.7%	0.1%
Other fiscal taxes	411	208	377	16.0%	12.6%	5.8%	5.0%	-5.3%	-3.9%	-5.3%	-3.9%
Social security contributions	57,779	28,081	55,856	3.6%	4.3%	4.7%	5.3%	4.4%	3.2%	4.6%	5.6%
Non fiscal revenue	17,390	8,131	16,105	0.5%	-0.8%	-3.8%	-6.4%	-12.7%	-10.7%	-19.6%	-11.5%
Capital revenues	621	392	755	-4.2%	-2.2%	-8.2%	-0.5%	2.0%	10.6%	18.7%	36.9%
Donations	15	170	323	-78.3%	-45.6%	-45.8%	-54.7%	782.4%	664.4%	267.5%	253.6%
EU preaccession funds	14,842	2,711	8,584	-33.8%	-1.1%	0.8%	11.7%	-17.7%	-18.2%	-16.0%	-10.8%
Other	0	11	-27	92.2%	74.1%	49.2%	n.a	n.a	n.a	n.a	n.a
Total expenditures	230,448	103,859	215,503	4.4%	4.4%	4.8%	3.8%	-2.9%	-3.8%	-2.3%	-0.3%
Current expenditures	212,653	99,540	201,165	5.4%	5.5%	6.3%	5.1%	0.7%	-0.6%	0.7%	2.3%
Compensation of public employees	47,786	23,889	47,091	19.9%	18.1%	14.7%	13.5%	2.6%	-4.4%	2.3%	3.4%
Operating expenditures	39,362	17,546	39,520	11.3%	6.9%	12.1%	12.0%	4.0%	7.3%	4.6%	5.7%
Interest paid	11,224	6,264	10,696	14.0%	0.7%	5.8%	0.4%	-20.4%	-3.1%	-6.4%	-1.0%
Subsidies	5,742	3,178	4,994	13.9%	9.3%	0.3%	-15.9%	-14.1%	-11.3%	-9.4%	-4.7%
Total transfers	107,262	48,423	98,201	-2.9%	0.9%	2.0%	1.8%	2.9%	0.6%	0.6%	1.9%
Transfers between units of public administration	549	501	1,085	84.0%	3.0%	6.7%	-25.4%	-35.7%	-32.3%	-55.6%	16.8%
Other transfers	11,817	6,582	10,913	15.2%	15.3%	11.1%	-2.6%	7.2%	2.4%	4.0%	3.3%
Projects financed by foreign non reimbursable funds	20,251	4,530	13,319	-45.3%	-18.3%	-8.1%	5.9%	-14.7%	-18.7%	-15.5%	-13.0%
Social benefits	71,513	35,198	69,535	1.0%	1.5%	1.9%	2.0%	4.2%	3.6%	3.7%	3.4%
Other	3,133	1,612	3,349	11.3%	16.4%	15.7%	8.5%	14.0%	0.4%	8.3%	8.8%
Expenses for programs with reimbursable funds	1,080	239	664	-38.3%	-36.9%	-46.3%	-46.2%	-58.6%	-61.7%	-49.4%	-46.2%
Capital expenses	17,796	4,807	15,510	-7.5%	-9.2%	-10.9%	-7.5%	-48.5%	-42.4%	-37.9%	-32.8%
Payments made in earlier years and recovered in the current year		-488	-1173	-16.6%	-8.2%	34.8%	52.4%	46.6%	38.5%	64.8%	53.9%
Excedent (+)/Deficit (-)	-14490	-3476	-12618	23.6%	-2.4%	13.6%	6.4%	-77.8%	-74.9%	-75.9%	-47.6%

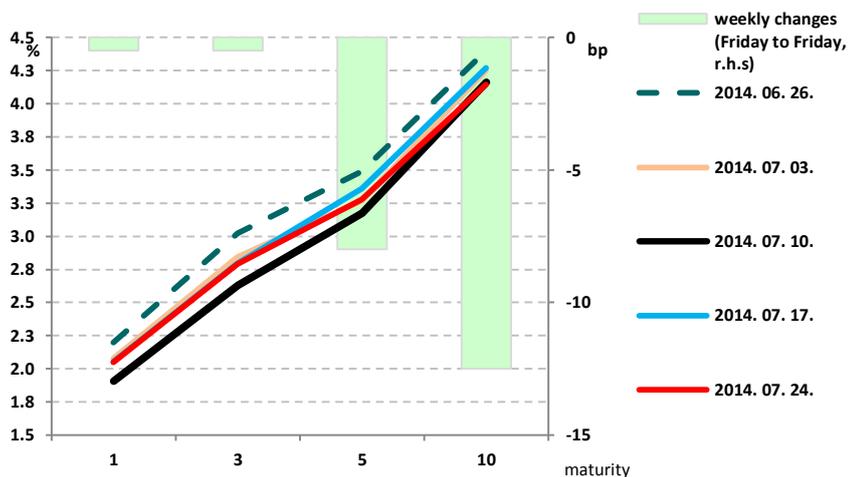
Source: Ministry of Finance

Government securities: new ISIN in JP Morgan Index

The yield curve dropped lower last week, especially at the long end, where the 5Y and 10Y bond yields shed off 10 and 17 bps respectively. This move took place for maturity horizons not perceived as completely exhausted considering the potential real yield gains. The market reaction was boosted by the news that **JP Morgan added a new domestic ISIN in its emerging market bond index** and it also included the Romanian securities in another index GBI-EM Global Diversified Investment Grade Index. **70% of RON outstanding government securities mature between 2014-2017** but in this maturity range, prices have already reached their highs.

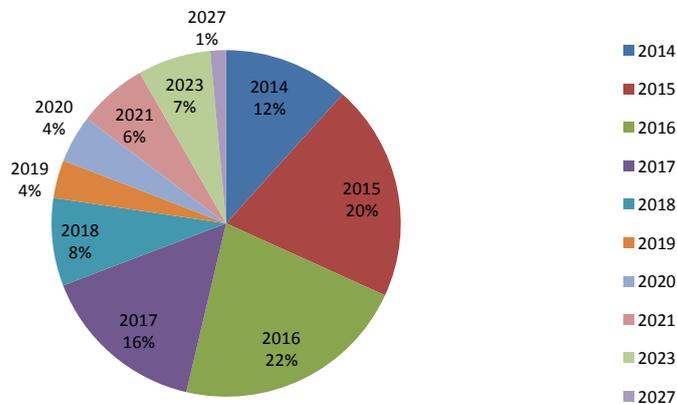
The Treasury sold bonds at still declining yields by 22-25 bps. The 4.3Y and 6.9Y bonds (residual maturity) had an average accepted yield of 3.1% and 3.88%, respectively. Demand was not as impressive as the previous week if we look at bid to cover ratio that stood below 2.

Yield curve over the past weeks (Central Bank fixing)



Source: NBR

Maturity structure of outstanding amounts for RON denominated debt



Source: Reuters

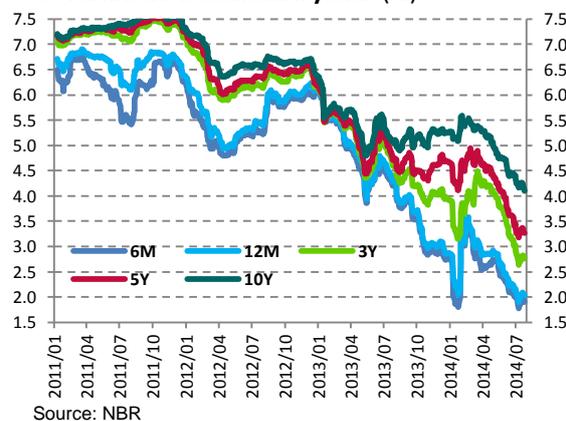
Date: 25.07.2014

RON GOVERNMENT SECURITIES				
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)	
6M	1.90	↓ -1	↓ -85	
12M	2.03	↓ -3	↓ -84	
3Y	2.77	↓ -4	↓ -115	
5Y	3.27	↓ -10	↓ -139	
10Y	4.10	↓ -17	↓ -118	

SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
GERROM 3Y	272	↓ -4	↓ -82	
GERROM 5Y	297	↓ -10	↓ -76	
GERROM 10Y	294	↓ -17	↓ -39	
3Y -5Y	50	↓ -6	↓ -24	
5Y -10Y	83	↓ -7	↑ 21	
3Y-10Y	133	↓ -13	↓ -3	
FLY 3-5-10	33	↓ -2	↑ 45	

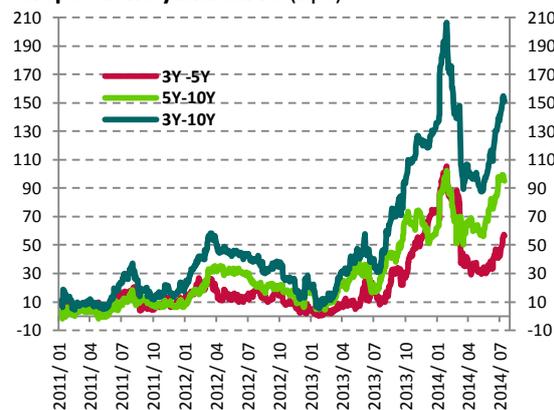
CDS MID SPREADS				
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)	
3Y EURO	71	↑ 2	↓ -46	
5Y EURO	122	↑ 2	↓ -49	

Government benchmark yields (%)



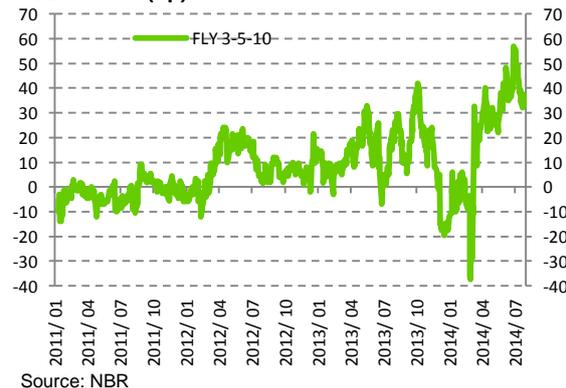
Source: NBR

Slope of the yield curve (bps)



Source: NBR

FLY 3-5-10 (bp)



Source: NBR

Auctions

T-bills auctions in July (in RON)

ISIN	Auction date	Settlement date	Maturity	Months	Indicative target amount (RON)
RO1415CTN0A3	28.07.2014	30.07.2014	29.07.2015	12	1.000.000.000

Source: The Ministry of Finance

Bonds auctions in July (in RON)

ISIN	Auction date	SSON auction date	Settlement date	Maturity	Years	Residual Maturity	Indicative target amount (RON)	Indicative target amount SSON* (RON)
RO1320DBN022	07.07.2014	08.07.2014	09.07.2014	29.04.2020	7.0	5.8	400.000.000	60.000.000
RO1316DBN053	10.07.2014	11.07.2014	14.07.2014	29.08.2016	3.0	2.1	400.000.000	60.000.000
RO1419DBN014	14.07.2014	15.07.2014	16.07.2014	24.06.2019	5.0	4.9	500.000.000	75.000.000
RO1215DBN073	17.07.2014	18.07.2014	21.07.2014	26.10.2015	3.0	1.3	300.000.000	45.000.000
RO1121DBN032	21.07.2014	22.07.2014	23.07.2014	11.06.2021	10.0	6.9	300.000.000	45.000.000
RO1318DBN034	24.07.2014	25.07.2014	28.07.2014	28.11.2018	5.0	4.3	300.000.000	45.000.000
RO1425DBN029	28.07.2014	29.07.2014	30.07.2014	24.02.2025	10.0	10.6	500.000.000	75.000.000

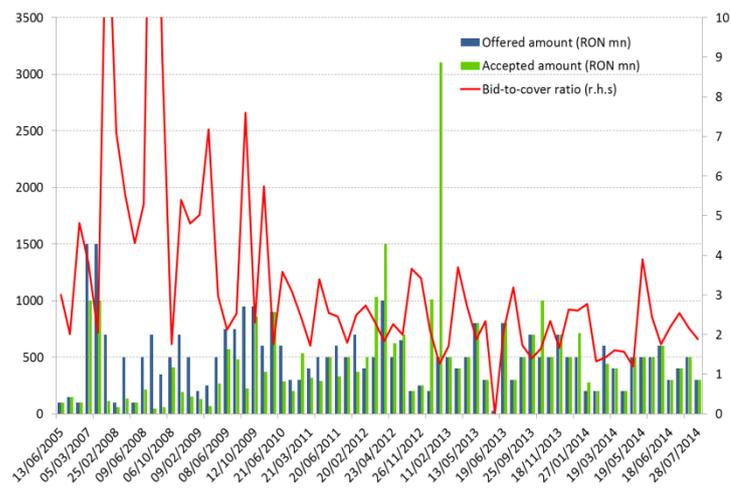
Source: The Ministry of Finance

Last week's auctions

	RO1121DBN032	RO1318DBN034
Offered amount (mn RON)	300	300
Total bids (mn RON)	974	565
Accepted amount (mn RON)	557	300
Average accepted yield (%)	3.88	3.10
Coupon	5.95	5.60

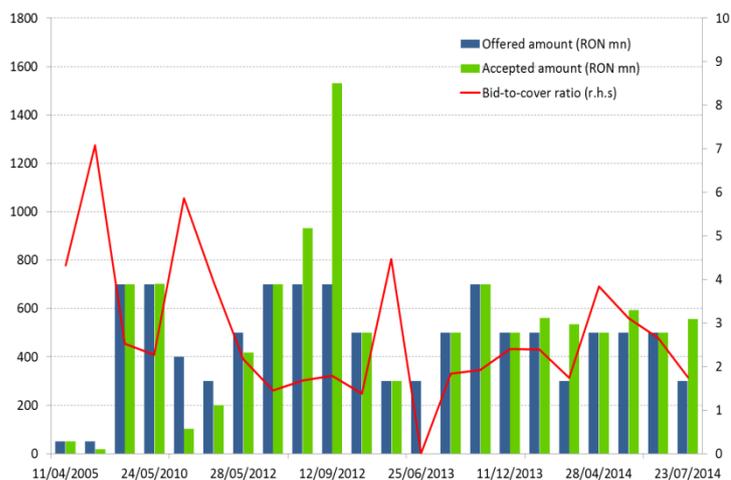
Source: NBR

5Y Auctions



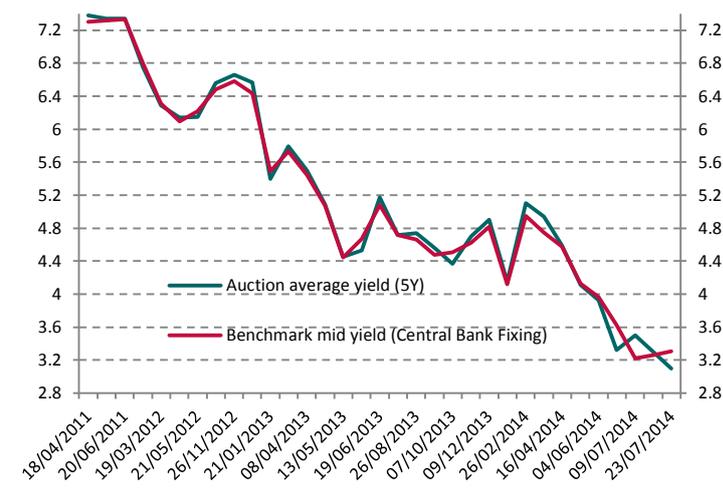
Source: NBR

7Y Interest rate



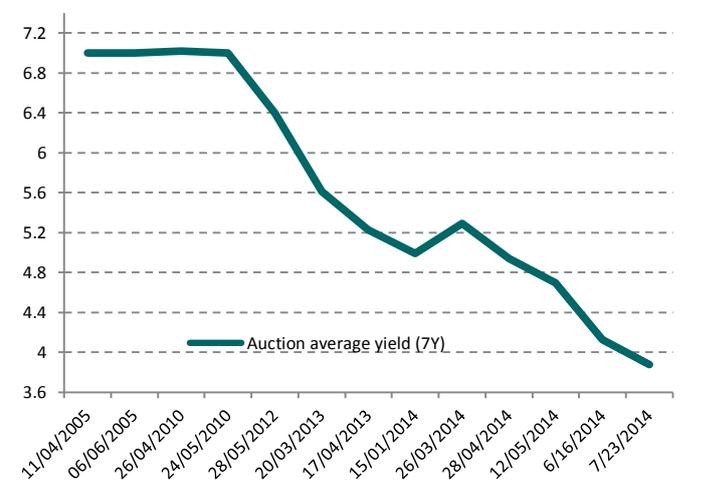
Source: NBR

5Y Interest rate



Source: NBR

7Y Interest rate

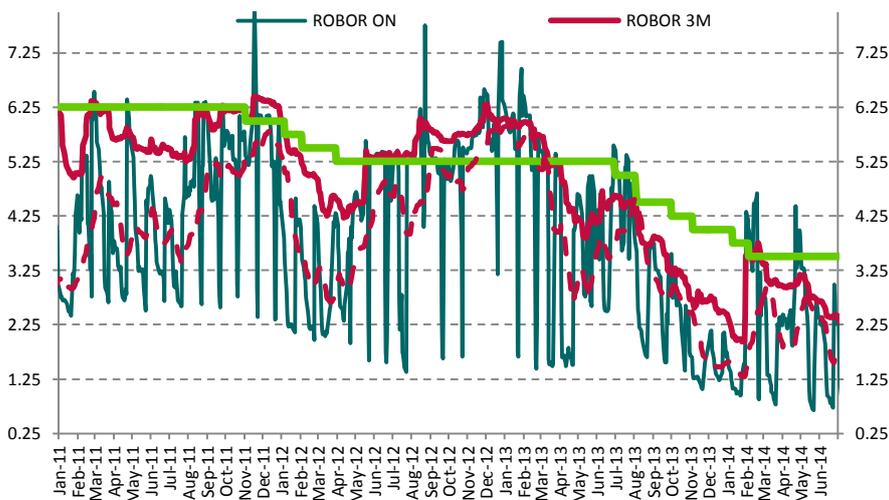


Source: NBR

MM: summer ease

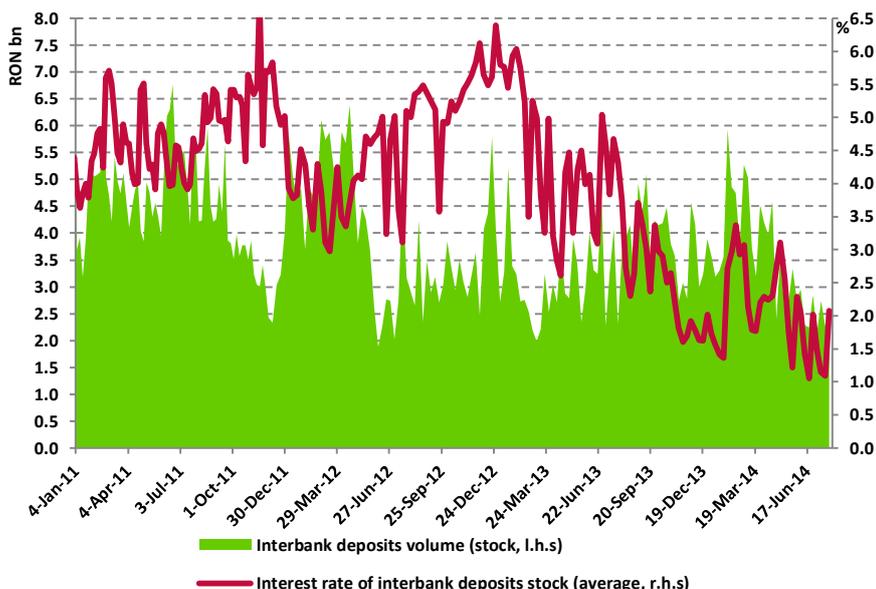
Liquidity conditions are at good levels and no pressure was felt last week, when corporate quarterly payments were due. The high government debt redemptions of July will help liquidity conditions in August as well, especially since the month has been slower from the auctions point of view in the past few years. With inflation rate posing little pressure in Romania and in the region as well, it is possible that the Central Bank will take further steps to ease the monetary policy as money market rates are persistently below the base rate. However the move should be carefully planned as the last quarter promises to be eventful due to domestic and external factors as well.

Most important MM rates



Sources: NBR

Interbank deposits and interest rate evolution



Sources: NBR

Date: 25.07.2014

MID INTEREST RATES			
	Value (%)	Weekly chg. (bp)	YTD chg. (bp)
repo rate	3.50	↔ 0	↓ -50
ROBOR ON	2.50	↑ 169	↑ 76
ROBOR 3M	2.20	↔ 0	↓ -24
ROBOR 6M	2.54	↓ -1	↓ -45
ROBOR 9M	2.63	↓ -1	↓ -47
ROBOR 1Y	2.67	↑ 1	↓ -48

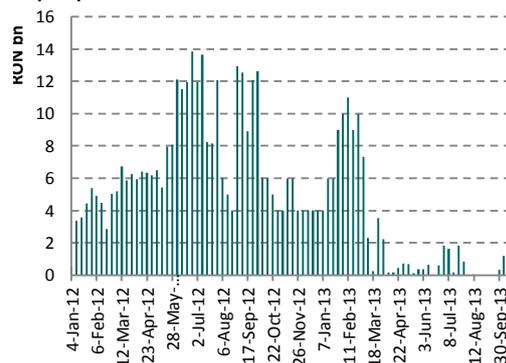
INTERBANK DEPOSITS			
	Value (mn RON)	Wly chg. (mn RON)	YTD chg. (mn RON)
outstanding	2,458.3	181.3	-2180.9

MID SWAP POINTS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
USDRON 1W	13	↑ 4	↑ 6
USDRON 1M	45	↓ -6	↑ 13
USDRON 3M	119	↓ -22	↑ 3
EURRON 1W	18	↑ 4	↑ 7
EURRON 1M	65	↓ -9	↑ 22
EURRON 3M	179	↑ 18	↓ -22

MID EUR BASIS SWAPS			
	Value (bp)	Weekly chg. (bp)	YTD chg. (bp)
EURRON 1Y	-70	↔ 0	↑ 40
EURRON 3Y	-60	↔ 0	↑ 50
EURRON 5Y	-60	↔ 0	↑ 50

Sources: Reuters

Repo operations since 2012



Sources: NBR

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