

# BALANCE OF PAYMENTS REPORT

2 March 2017

***Imbalance indicators point to a favourable picture; the modest CA deficit is offset by EU funds and FDI flows, helping external debt to fall***

- The main indicators of imbalances paint a healthy picture about Romania, with the external financing capacity measures remaining above the zero threshold at the end of 2016 (see Chart 1). This was primarily helped by the cautious behaviour of the private sector, offsetting the negative effects coming from loose fiscal policies (Chart 2). The EFC1 indicator finished last year with 0.1% surplus compared to GDP, after inflows from EU funds helped the capital balance to compensate the deficit of the current account. Meanwhile, the EFC2 (EFC1 plus net errors and omissions), probably the first best indicator for underlying dynamics, stood at even higher levels, at 1.3% of GDP, according to our calculation based on the provisional data of the central bank.
- At the same time, the country's current account deficit (CA) remained at relatively low levels, at 2.45%, up from 1.21% in the previous year (see Chart 3). The widening CA gap was mostly the result of a more significant shortfall in the balance of goods, as the strong domestic demand led to the acceleration of imports, while exports were unable to keep pace with it, given a slight slowdown in the eurozone economy last year. Simultaneously, the negative balance of primary incomes also put some downward pressure on the CA, after companies paid out larger dividends to their foreign shareholders than a year earlier. Worker's remittances seemingly decreased as well in 2016, pulling back the line of secondary incomes, and consequently negatively affecting the CA. On the positive side, the surplus of services inched up modestly, fuelled mainly by the export of IT&C services. We recall that this sector gained more and more importance in the Romanian economy in recent years, reaching around 6% contribution to the country's GDP, outpacing agriculture by a considerable margin last year.
- Further good news is that net direct investments pointed to a favourable evolution in 2016, reaching their highest level in nominal terms since 2009. Meanwhile, it remained at a healthy level of around 2.3% of GDP (Chart 5), more or less in line with other countries of the CEE region.
- Sustained by the positive external financing capacity and FDI flows, gross external debt without intercompany loans (which are more FDI-like than debt) continued to shrink (but indeed at a slower pace in the latest period; see Chart 6). The main driver behind the drop in recent quarters remained the banking sector, whose debt contracted by 0.7 percentage points in the last three months of 2016, and by 2.4 pps versus the end of 2015. This came after financial institutions remarkably consolidated their positions, supported also by the large fall in the non-government loan-to-deposit ratio (Chart 8).
- Looking ahead, we expect that the current account deficit may increase in 2017 too, first of all, as imports' growth could remain robust on the back of strong domestic demand. It may be worth noting that households' consumption is expected to get support from a new package of fiscal stimulus measures too. At the same time, with the signs of inflation returning at global level, imports may become more expensive as well (Chart 10), while the outlook of exports' growth appears to be rather limited by the modest recovery of the eurozone and due to some competitiveness issues on the domestic front.
- Nevertheless, we think that given the low level of Romania's external debt, the robust inflows from EU funds and FDIs, together with the more than adequate FX reserve (Chart 9), the country is on a sustainable path. In our view, this is valid even though the budget deficit will show a modest slippage from the 3% target this year (our base scenario at this moment). Of course, a prudent approach concerning the government budget remains crucial in the medium term.

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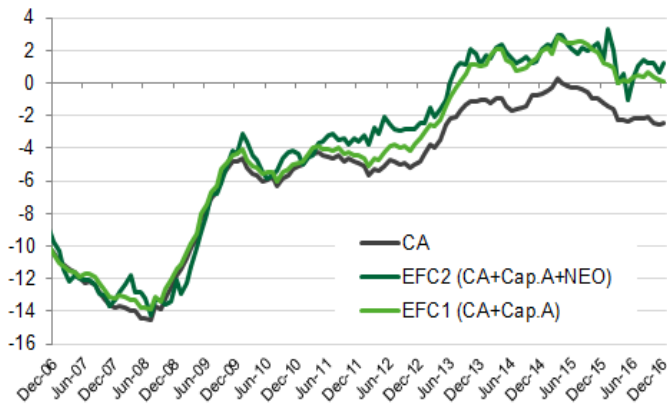
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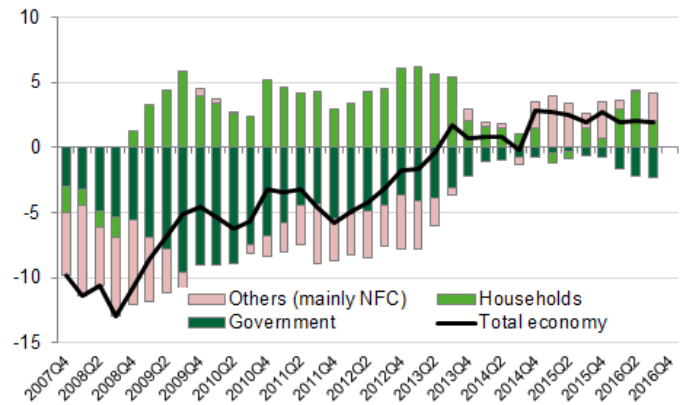
Chart set:

**Chart 1: Main indicators of external balance**  
(as % of GDP, 12M rolling)



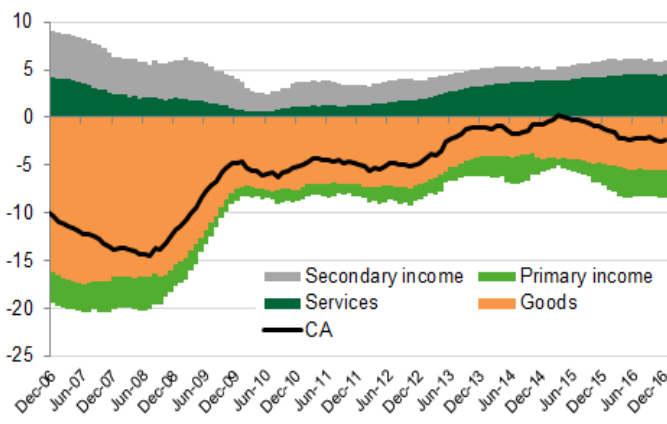
Sources: NBR, NIS, OTP Research  
 Note: **EFC1** (External financing capacity 1) = Current account + Capital account; **EFC2** (External financing capacity 2) = EFC1 + Net errors and omissions

**Chart 2: Net financing capacity of the main sectors and the whole economy**  
(as % of GDP, 4Q rolling)



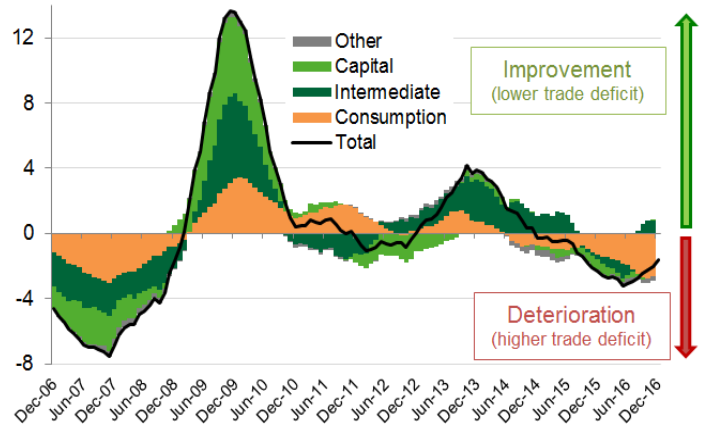
Sources: NBR, NIS, OTP Research  
 Note: Q4 2016 data is not available yet

**Chart 3: Current account by its main components**  
(as % of GDP, 12M rolling)



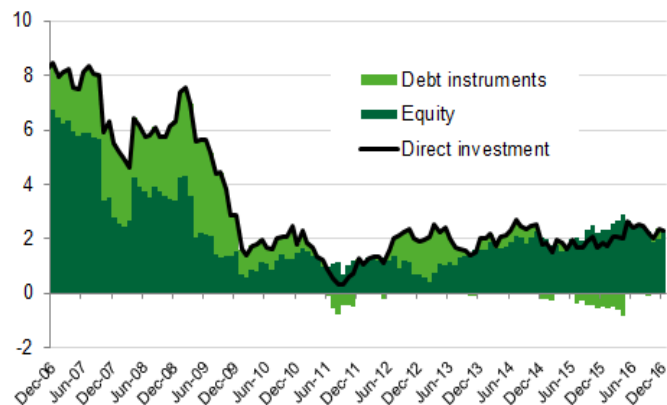
Sources: NBR, NIS, OTP Research

**Chart 4: Change in the balance of goods by main product types**  
(EUR bn, 12M rolling)



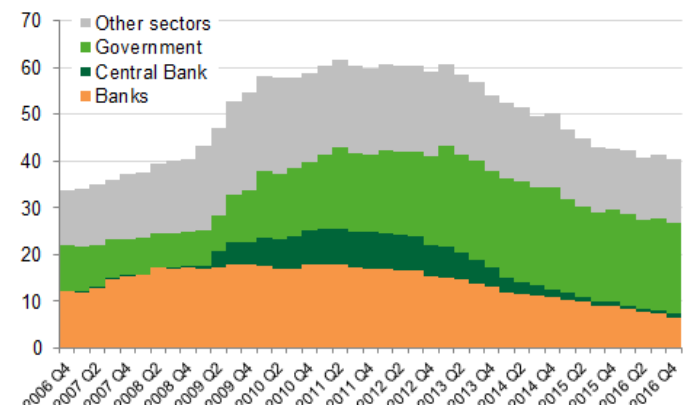
Sources: Eurostat, OTP Research

**Chart 5: Net direct investment**  
(as % of GDP, 12M rolling)



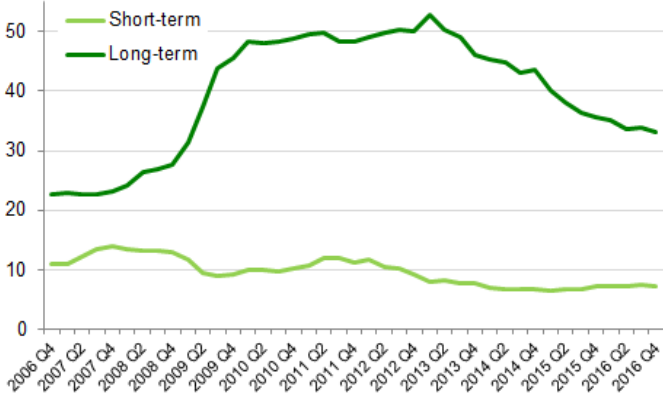
Sources: NBR, NIS, OTP Research

**Chart 6: Gross external debt by sectors**  
(as % of GDP)



Sources: NBR, NIS, OTP Research  
 Note: without intercompany lending; based on BPM5 methodology until 2012 Q4

**Chart 7: Gross external debt by tenor (as % of GDP)**



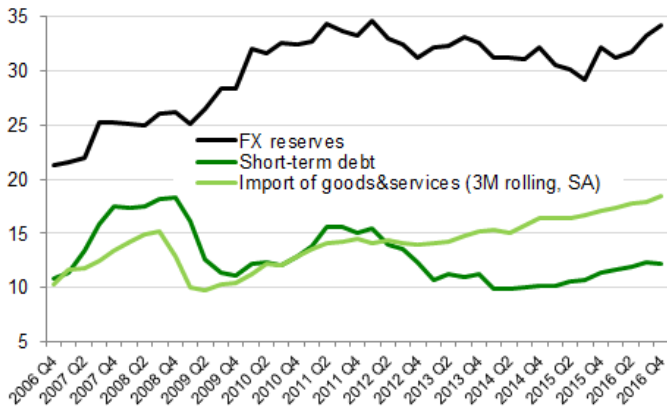
Sources: NBR, NIS, OTP Research  
Note: without intercompany lending

**Chart 8: Loan-to-deposit ratio in the banking sector (% excl. government loans and deposits)**



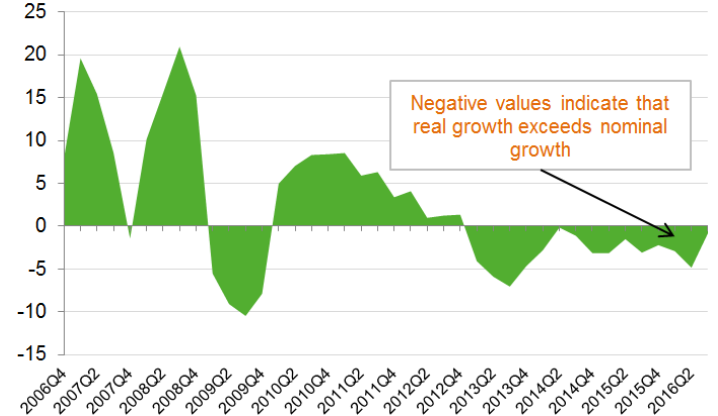
Sources: NBR, OTP Research

**Chart 9: Reserves and reserve adequacy rules (EUR bn)**



Sources: NBR, NIS, OTP Research  
Note: without intercompany lending

**Chart 10: Real vs. nominal growth of imports (YoY %)**



Sources: NBR, NIS, OTP Research

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