otp Research

# GDP REPORT

*9 March 2018*

## *Relatively soft headline data, but still strong underlying growth; moderation may come in 2018*

- The NIS has confirmed Romania's GDP growth rate at 6.9% YoY (gross data; see Chart 1) and 0.6% QoQ (seasonally and working day adjusted data) in the last quarter of 2017. These growth paces mark a deceleration compared to Q3's cheering figures (8.8% YoY / 2.4% QoQ). In addition, the headline data also fell short of the market expectation (7.0% YoY, according to a Reuters survey) as well as ours (7.6% YoY) due to weaker agriculture output and falling inventories. On the other hand, the underlying performance of the economy surprised us on the upside, with the non-farm private sector GDP growing by 7.2% YoY, following Q3's 7.1% YoY advance (Chart 2). On QoQ basis, value added in the non-farm private sector increased by 2.2%, up from 1.4% a quarter earlier. Simultaneously, domestic demand was also somewhat stronger than we had expected, with household consumption and fixed investment posting double-digit growth paces.
- In 2017, Romania's economy grew by 7.0%, the report of the NIS also showed. This was the fastest increase since the outburst of the financial crisis as well as one of the largest gains in the EU. Last year's pick-up came after an already impressive 4.8% expansion in 2016. We recall that Romania's economy is in the mature phase of the business cycle, with a series of steroids propelling the country to fire on all cylinders. Loose fiscal policies boosted consumption growth, monetary conditions were unusually accommodative, while the rebound of the EZ economy and favourable weather conditions helped too. Nevertheless, it seems that the peak is over and slower growth rates may come, as the positive impact of several one-off factors is set to fade. It is important to note that on the back of the eye-watering GDP figures, miscalibrated government policy, widening current account gap and rapidly rising inflation, overheating risks also escalated.
- In Q4, household consumption expenditures continued to grow swiftly (12.7% YoY / 2.2% QoQ versus 12.4% YoY / 3.2% QoQ a quarter earlier), remaining the key driver of the economy (Charts 3&5). In the light of moderating real wage dynamics (Chart 6), falling consumer confidence (Chart 7) and less impressive high-frequency economic data (Chart 8), we had expected a somewhat weaker outturn for Q4. In our previous report, we noted that the excellent agricultural harvest may have boosted own consumption in rural areas in Q3. It is likely that this positive effect persisted in Q4 too. Nevertheless, we think that a slowdown in household expenditures should come already at the beginning of this year.
- The good news is that fixed investment picked up sharply (Charts 3 & 5) in Q4, after the disappointment in 2016 and H1 2017, as sluggish public investment weighed on the indicator. The more detailed statistics revealed that investment both in new construction and equipment increased in annual comparison, but the largest advance was registered at other capital expenditures (Chart 9). The latter item covers a large range of investments, including expenditures for geological and drilling works, for research and design studies on investment objectives, as well as for the services related to property transfer. We think that the slowly but still improving loan flow to companies may have played a role in the recovery of private investments in 2017. Undoubtedly, corporate credit lost momentum last December, but this was mainly the result of portfolio cleaning efforts of commercial banks. The latest government budget statistics pointed to somewhat higher capital expenditures at the end of 2017, while EU fund absorption provided early signs of a recovery, after achieving a breakthrough in the accreditation process of the 2014-2020 operational programmes. Overall, we are optimistic about the outlook of investment in 2018, but given the stretched government budget, uncertainties around the fiscal policy, and rising borrowing costs, the risks are tilted to the downside.
- In the last quarter of 2017, net exports was again negative contributor to GDP growth (Chart 3). Despite the revival of the eurozone economy, exports were not able to keep pace with domestic-demand-fuelled imports. The general picture could be similar this year too. In 2018, exports may perform well as the global economy maintains momentum. In addition, the start of production of a new Ford model and the official launch of the new Dacia Duster may also help. On the other hand, with softer but still robust consumption and recovering investments, imports' growth most likely will outpace that of exports this year too.


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- On the production side, agriculture explained Q4's slowdown of the headline GDP (Chart 4), but it is important to note that this came after the sector's excellent performance a quarter earlier. Market services remained the primary driver of the economy, with all of its sub-sectors pointing to increases. Simultaneously, industry accelerated as the growth rate of production for the domestic market started to go up (Chart 10). At the same time, construction output was sluggish, pointing to a marginal increase in Q4. We recall that in 2017 the performance of the construction sector was dragged down by disappointing public investments, offsetting the revival of the residential segment.
- Timelier sentiment indicators (Chart 11) as well as softening retail sales data suggest that Romania's economy may lose steam at the beginning of 2018. This would be in line with our expectations. We reiterate that the data for the beginning of 2018 are worth watching, as the impact of tax changes (transferring the burden of social contributions from employers to employees) is also set to appear.
- In our previous report, we noted that miscalibrated government policies as well as the failure to achieve quality improvement in the case of education and health, are likely to transform into a bottleneck for the country's growth outlook. Nonetheless, the potential negative effects could come from demographic trends too. Due to emigration waves and lower birth rate, Romania's resident population registered double-digit loss in the period of 2016-2000 (Chart 12). Only a few counties, mostly the large economic centres, were able to maintain or marginally increase resident population (Chart 13). In this context, sound fiscal policies are even more important in order to preserve the country's growth potential.
- Summing it up, we think that Romania's GDP could increase by 4.2% this year (revised marginally upward owing to stronger-than-expected underlying momentum). In 2019, economic growth may decelerate to 3.8%.

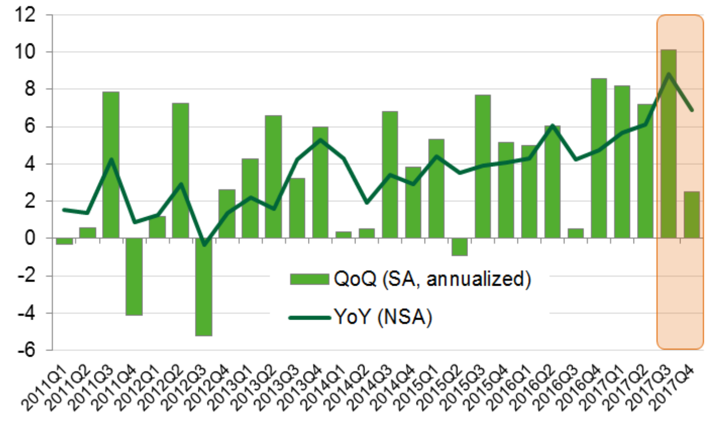
**Main macro forecasts**

| Key economic indicators | | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018F | 2019F |
|---|---|---|---|---|---|---|---|---|---|---|
| Real GDP | % | 2.0 | 1.2 | 3.5 | 3.1 | 4.0 | 4.8 | 7.0 | 4.2 | 3.8 |
| Final consumption of households | % | 1.3 | 2.4 | -2.4 | 4.4 | 5.7 | 7.4 | 8.8 | 4.9 | 3.7 |
| Cons. expenditure of housh. | % | 1.4 | 1.7 | 2.6 | 4.2 | 5.8 | 7.9 | 10.3 | 5.3 | 4.2 |
| Public consumption | % | 0.2 | 0.3 | -4.6 | 0.8 | 0.2 | 3.1 | 1.6 | 1.3 | 1.4 |
| Investment | % | 6.2 | 3.6 | -5.4 | 3.2 | 7.4 | -2.0 | 5.4 | 5.0 | 4.7 |
| Exports | % | 11.9 | 1.0 | 19.7 | 8.0 | 4.6 | 8.7 | 9.5 | 8.6 | 7.8 |
| Imports | % | 10.1 | -1.8 | 8.8 | 8.7 | 8.0 | 9.8 | 11.1 | 9.1 | 7.9 |
| Consumer prices | % annual avg | 5.8 | 3.3 | 4.0 | 1.1 | -0.6 | -1.5 | 1.3 | 4.1 | 2.9 |
| Government sector balance | in % of GDP | -5.4 | -3.7 | -2.1 | -1.4 | -0.8 | -3.0 | -3.0 | -3.0 | -2.9 |
| Public debt | in % of GDP | 34.2 | 37.3 | 37.8 | 39.4 | 38.0 | 37.6 | 36.5 | 36.5 | 36.9 |
| Current account | in % of GDP | -5.0 | -4.8 | -1.1 | -0.7 | -1.2 | -2.1 | -3.5 | -3.9 | -4.0 |
| Key interest rate | % annual avg | 6.2 | 5.3 | 4.8 | 3.3 | 1.9 | 1.8 | 1.8 | 2.4 | 3.0 |
| Key interest rate | % end of period | 6.00 | 5.25 | 4.00 | 2.75 | 1.75 | 1.75 | 1.75 | 2.75 | 3.25 |
| Nominal GDP | RON bn. | 562.1 | 595.4 | 637.5 | 668.1 | 712.7 | 762.3 | 856.4 | 933 | 1002 |
| Unemployment | % | 7.2 | 6.8 | 7.1 | 6.8 | 6.8 | 5.9 | 5.0 | 4.5 | 4.4 |
| Nominal wage growth | % | 4.1 | 4.2 | 4.8 | 7.6 | 9.8 | 9.9 | 14.8 | 10.2 | 9.1 |
| Real wage growth | % | -1.6 | 0.8 | 0.8 | 6.5 | 10.4 | 11.7 | 13.3 | 5.9 | 6.0 |
| Nominal GDP | EUR bn. | 132.6 | 133.6 | 144.3 | 150.3 | 160.3 | 169.8 | 187.5 | 201 | 218 |

*Sources: NIS, NBR, Eurostat, OTP Research*

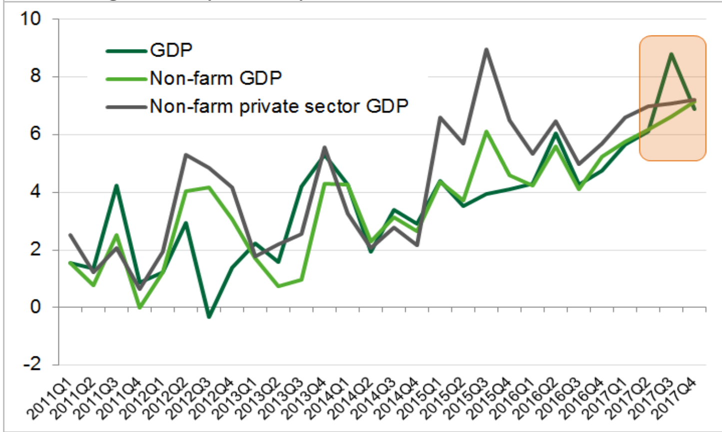
## Chart set:

**Chart 1: Summary chart of GDP growth** (%)



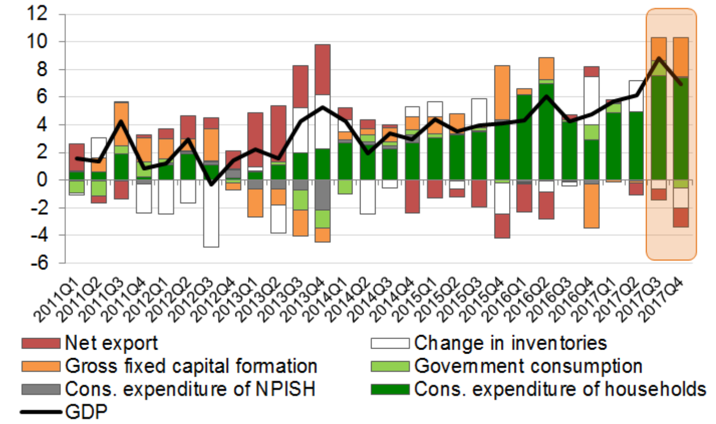

*Sources: NIS, OTP Research*

**Chart 2: GDP vs. non-farm and non-farm private sector growth** (YoY, %)



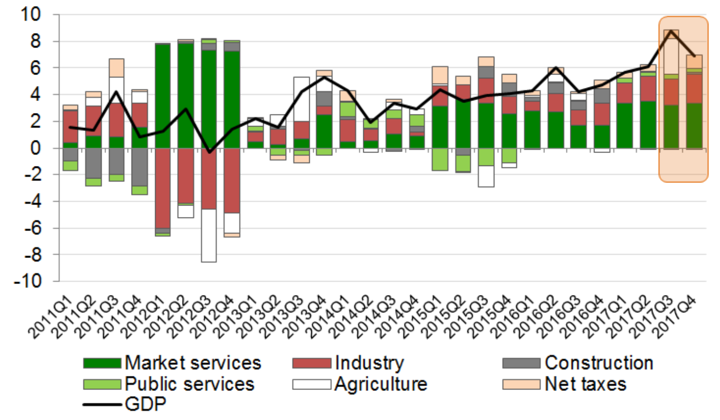

*Sources: NIS, OTP Research*

**Chart 3: Decomposition of GDP growth by expenditure-side items** (%)



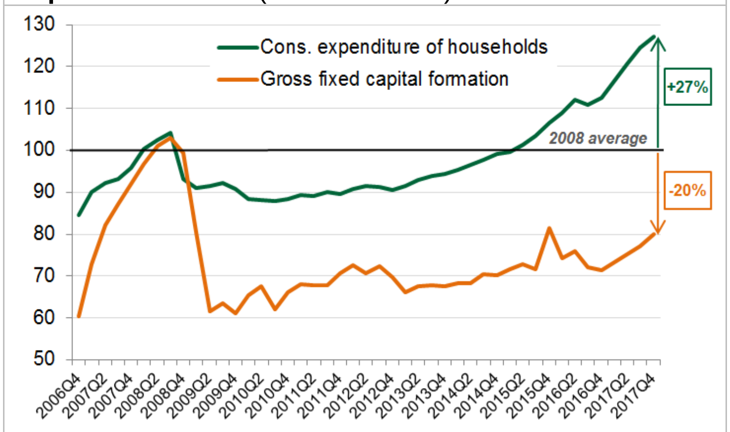

*Sources: NIS, OTP Research*

**Chart 4: Decomposition of GDP growth by production-side items** (%)



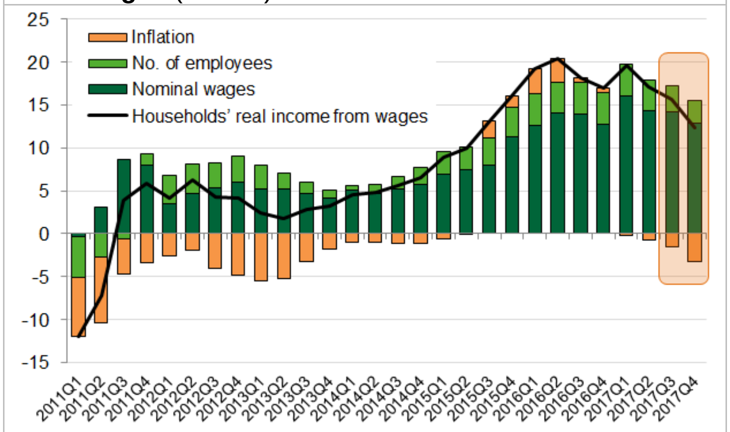

*Sources: NIS, OTP Research*

**Chart 5: Evolution of households' consumption vs. capital investment** (2008 av. = 100)



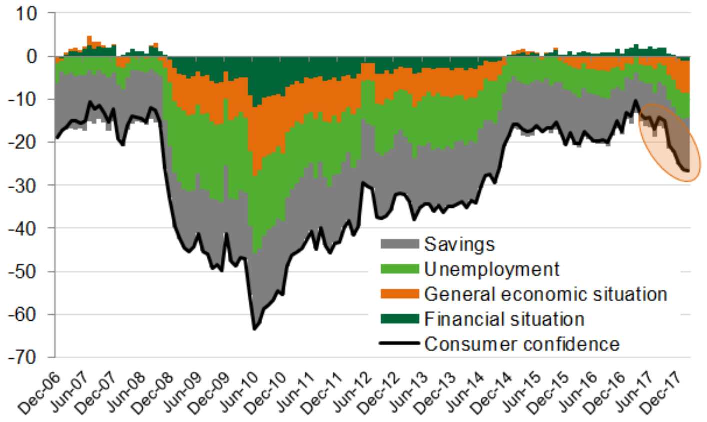

*Sources: NIS, OTP Research*

**Chart 6: Decomposition of households' real income from wages** (YoY %)



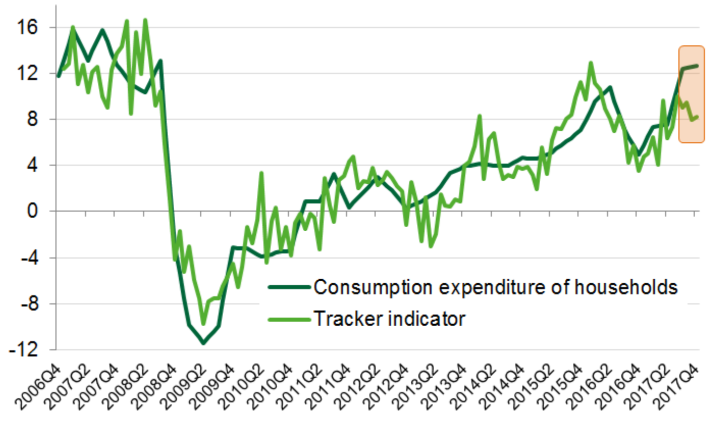

*Sources: NIS, OTP Research*

**Chart 7: Decomposition of consumer confidence indicator** (balance of opinions)



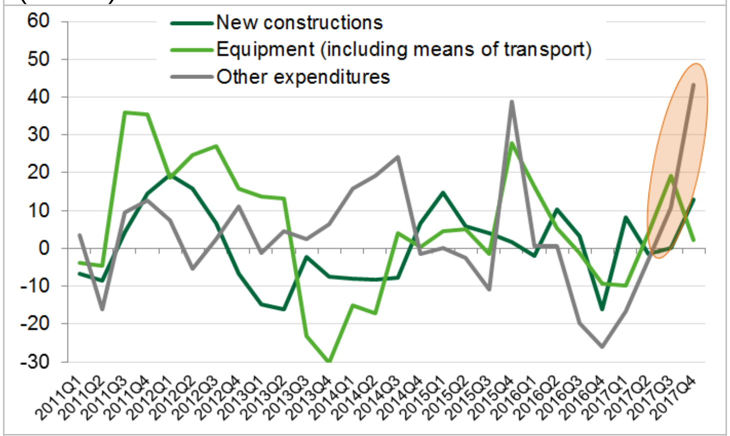

*Sources: EC, OTP Research*
*Note: the components of the consumer confidence indicator reflects the expectation of households over the next 12 months*

**Chart 8: Households' consumption vs. its tracker indicator** (YoY%, monthly data)



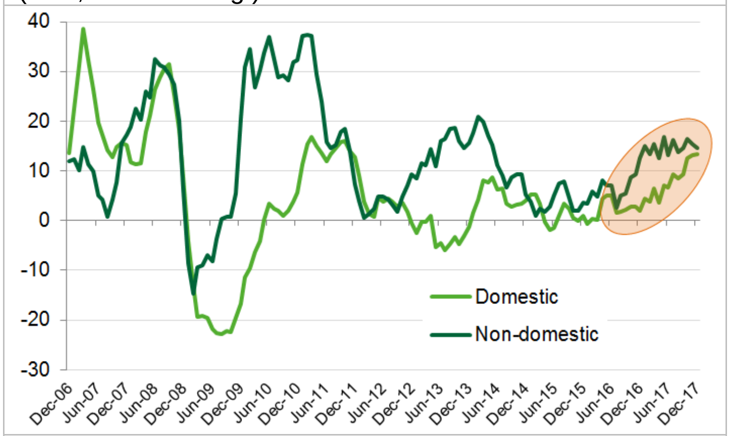

*Sources: NIS, OTP Research*
*Note: the consumption tracker is an in-house composite indicator based various high-frequency indicators, including among others retail sales and passenger car registration data*

**Chart 9: Net investments**
(YoY %)



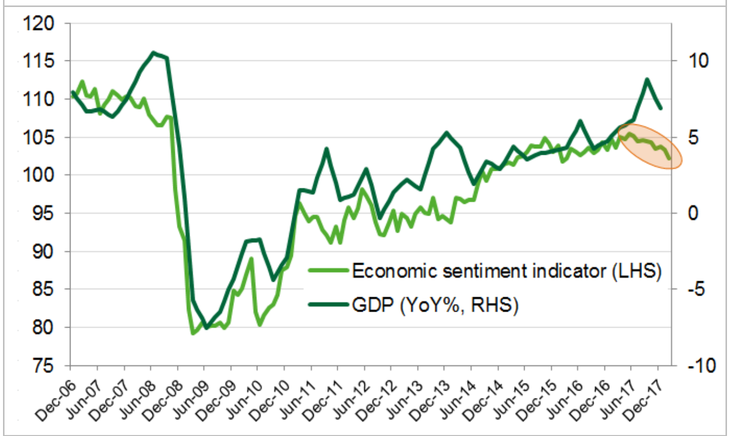

*Sources: NIS, OTP Research*

**Chart 10: Turnover value indices in industry**
(YoY, 3M mov. avg.)



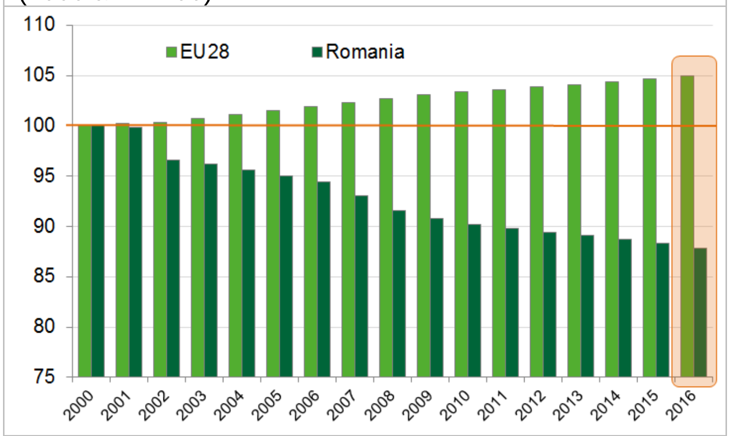

*Sources: NIS, OTP Research*

**Chart 11: GDP growth vs. economic sentiment indicator**




*Sources: NIS, EC, OTP Research*

**Chart 12: Population of Romania vs. EU28**
(2000 av. = 100)




*Sources: Eurostat, OTP Research*

**Chart 13: Population change since 2000**
(2016 vs. 2000, %)


| Rank | County | Change |
|---|---|---|
| 1 | Hunedoara | -24.3 |
| 2 | Tulcea | -23.1 |
| 3 | Teleorman | -22.8 |
| 4 | Neamt | -22.5 |
| 5 | Braila | -21.9 |
| 6 | Mehedinti | -21.8 |
| 7 | Bacau | -20.6 |
| 8 | Caras-Severin | -20.5 |
| 9 | Galati | -19.7 |
| 10 | Olt | -19.2 |
| 11 | Vaslui | -17.5 |
| 12 | Gorj | -17.4 |
| 13 | Vâlcea | -16.8 |
| 14 | Alba | -16.0 |
| 15 | Vrancea | -15.6 |
| 16 | Salaj | -15.5 |
| 17 | Botosani | -15.4 |
| 18 | Buzau | -15.1 |
| 19 | Dolj | -14.2 |
| 20 | Prahova | -13.9 |
| 21 | Satu Mare | -13.5 |
| 22 | Bistrita-Nasaud | -13.5 |
| 23 | Ialomita | -13.3 |
| 24 | Brasov | -12.4 |
| 25 | Suceava | -12.4 |
| 26 | Maramures | -12.0 |
| 27 | Arges | -11.7 |
| 28 | Calarasi | -11.4 |
| 29 | Arad | -11.2 |
| 30 | Covasna | -11.0 |
| 31 | Harghita | -10.2 |
| 32 | Sibiu | -10.0 |
| 33 | Mures | -9.9 |
| 34 | Constanta | -8.9 |
| 35 | Dâmbovita | -8.6 |
| 36 | Bihor | -8.5 |
| 37 | Giurgiu | -6.6 |
| 38 | Iasi | -5.7 |
| 39 | Cluj | -2.5 |
| 40 | Bucuresti - Ilfov | 0.2 |
| 41 | Timis | 1.2 |

*Sources: Eurostat, NIS, OTP Research*

## Disclaimer