BANCA NAȚIONALĂ A ROMÂNIEI

Romania: macroeconomic picture and finance (banking)

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Dynamics after 2009

- Period of huge uncertainty in Europe: economic and geopolitical risks
- GDP recovered, growth rate up, output gap to turn positive in 2016
- Massive reduction of imbalances, but new budget pressures…
- Negative inflation negative due to fiscal measures, domestic consumption has firmed up
- Nominal convergence criteria are met, but more is at stake…
- EU funds absorption improved, but still much to accomplish
- Transmission of monetary policy better; *policy space* available
- Lower contagion risk in the banking sector; NPLs reduced

…sustainability of positive developments needs further proof and more structural reforms have to take root

General government budget deficit

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016*
Budget deficit (% of GDP) cash	-0.7	-1.4	-3.1	-4.8	-7.3	-6.3	-4.2	-2.5	-2.5	-1.7	-1.2	-2.8
Budget deficit (% of GDP) ESA	-1.2	-2.2	-2.9	-5.6	-9.1	-6.9	-5.4	-3.2	-2.2	-1.4	-1.1	-3.0
Primary deficit (% of GDP)**	0.0	-1.4	-2.2	-5.0	-7.5	-5.1	-3.7	-1.2	-0.5	0.2	0.3	-1.5
Structural deficit* (% of GDP)**	-2.5	-4.4	-5.2	-8.6	-8.8	-5.8	-3.0	-2.1	-1.2	-0.7	-1.0	-3.0

* Projections for 2016 according to Ministry of Public Finance (cash deficit, primary deficit) and European Commission - Winter 2016 Economic Forecast (ESA deficit, structural deficit)

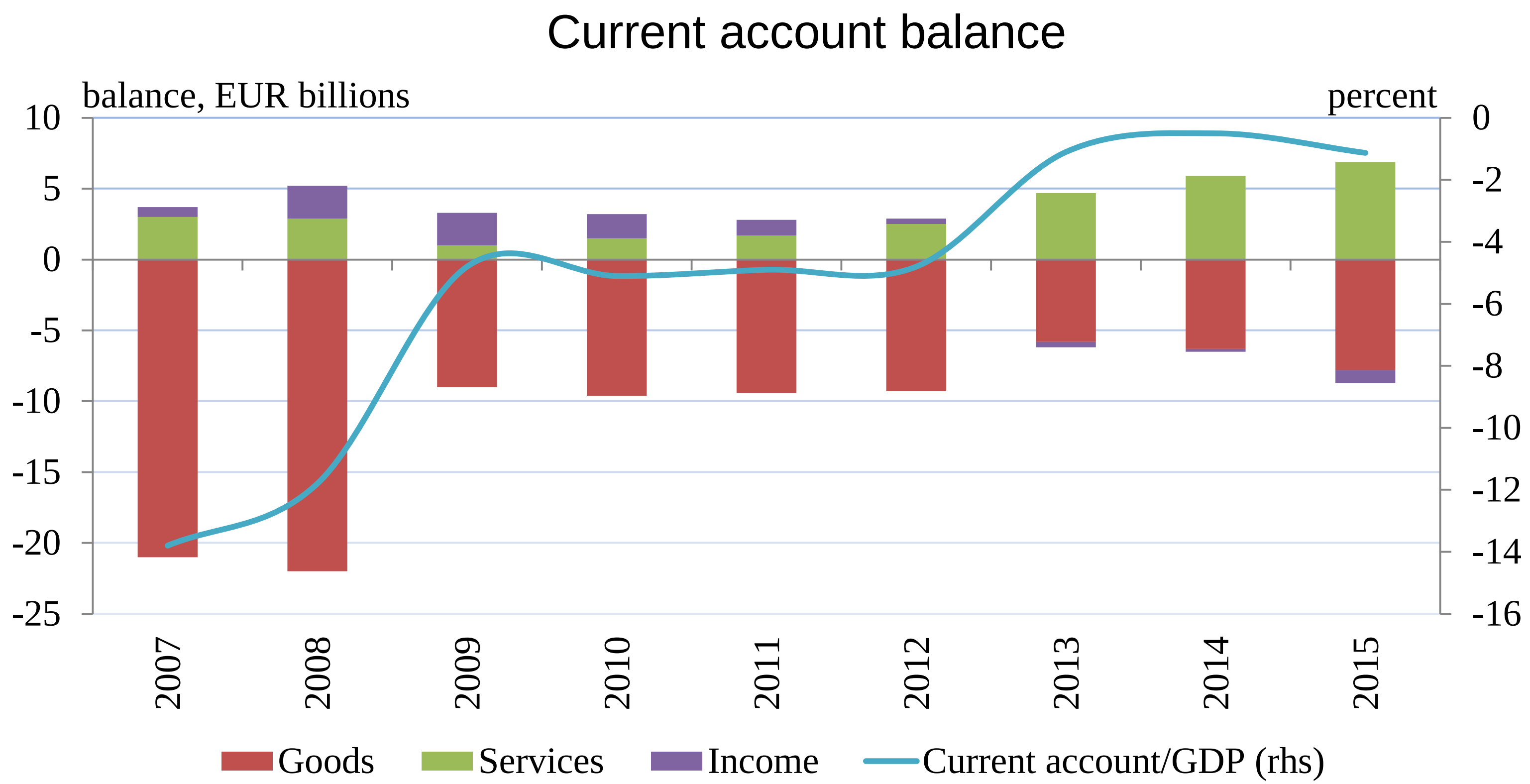
** The primary deficit is the budget deficit before including interest payable.

*** A structural deficit occurs if the fiscal balance is in deficit when computed at potential output level.

Source: MPF, European Commission, Eurostat

External balance improved

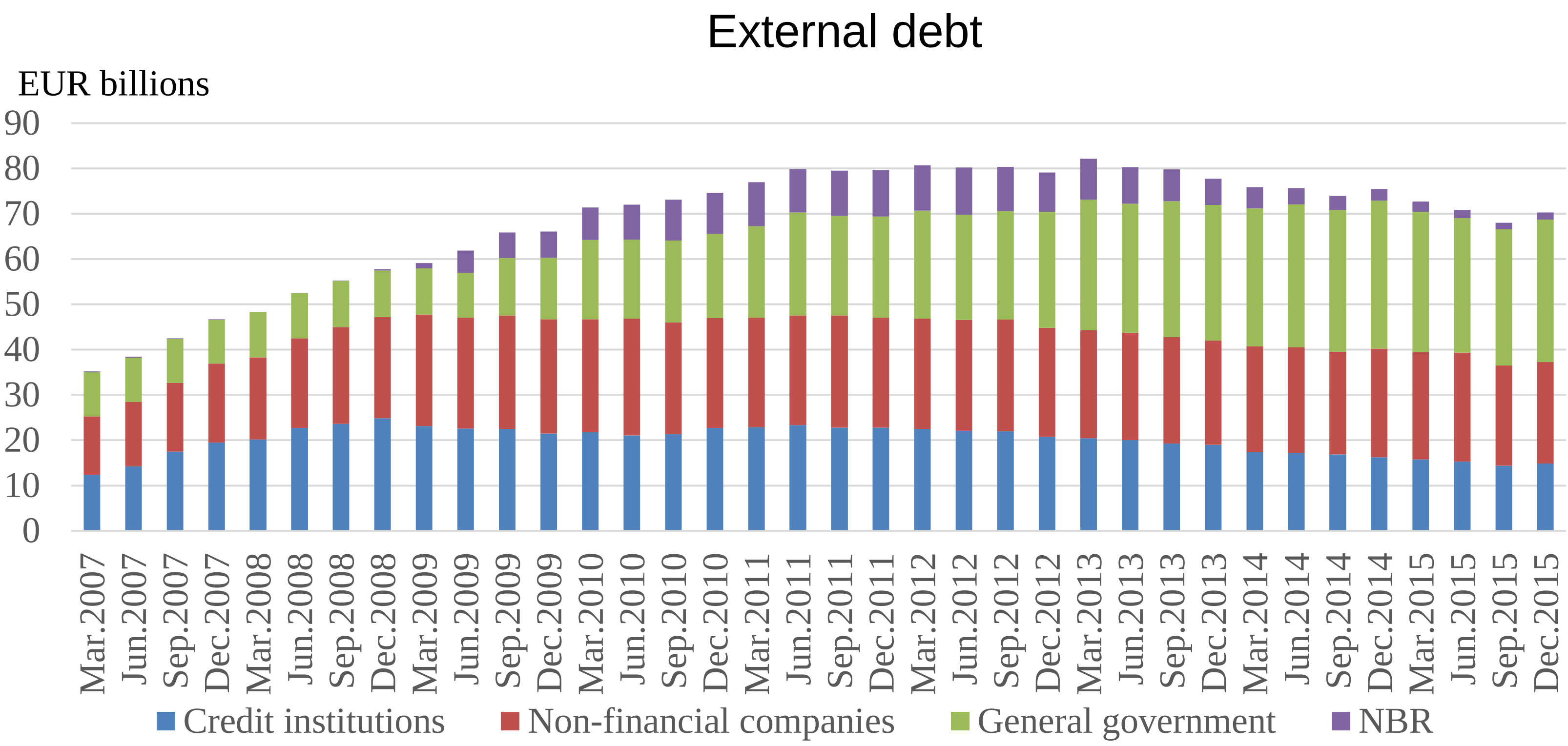
- **The current account deficit narrowed significantly since 2009, but resumed growth in 2015 as domestic consumption grew strongly**
- **The trade surplus in services soared over the past years, driven by transport and IT**



Source: NBR

External debt declined

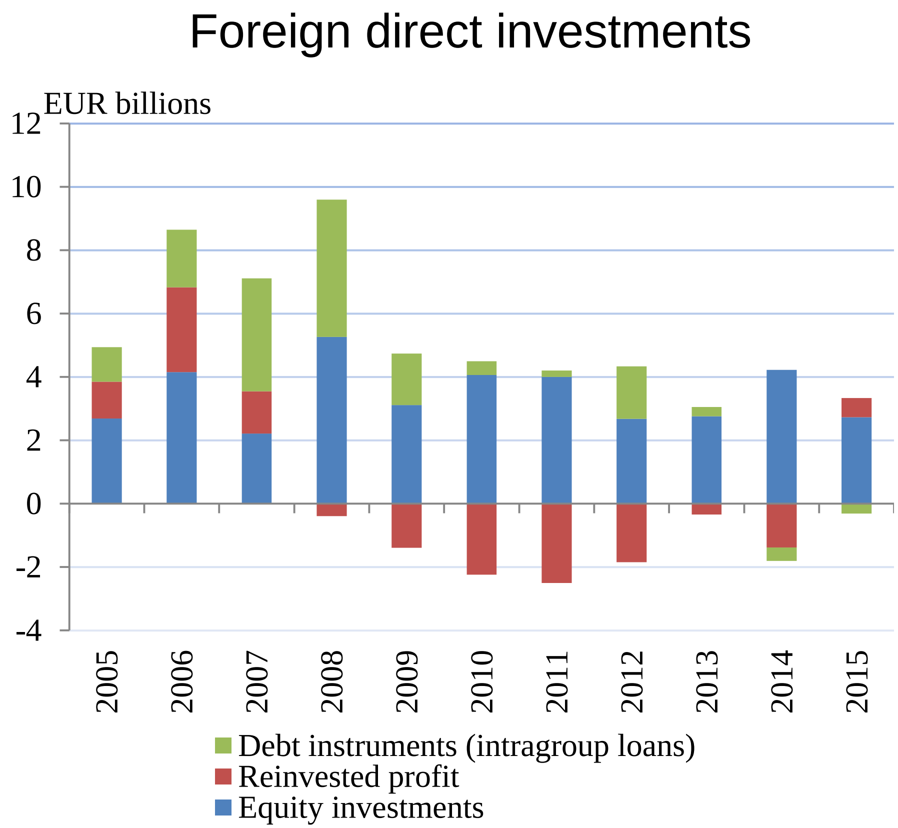
- **External public debt increased in the aftermath of the international crisis in tandem with gradual deleveraging in the private sector**
- **NBR reimbursed the IMF loans it got in 2009 almost entirely**

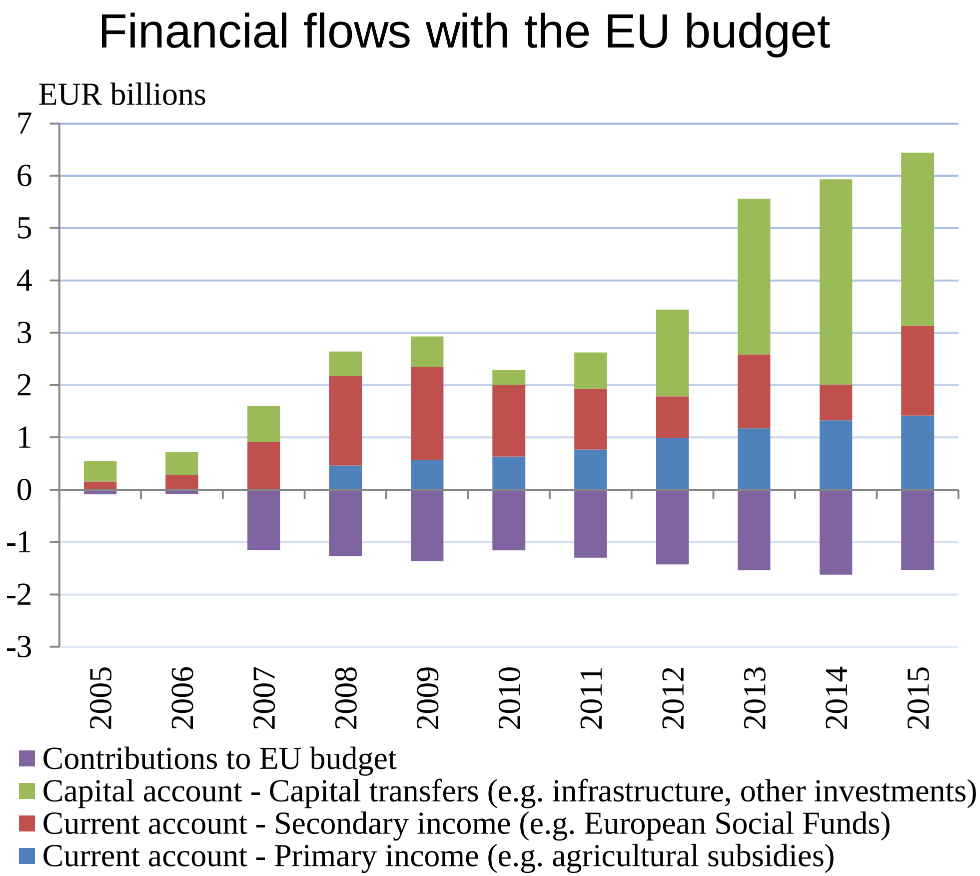


Source: NBR

Larger absorption of EU funds offsets lower FDIs

- **EU funds absorption improved significantly since 2013, mainly capital transfers**
- **FDIs are still low, yet reinvested profit in 2015 signals higher confidence in local economy**

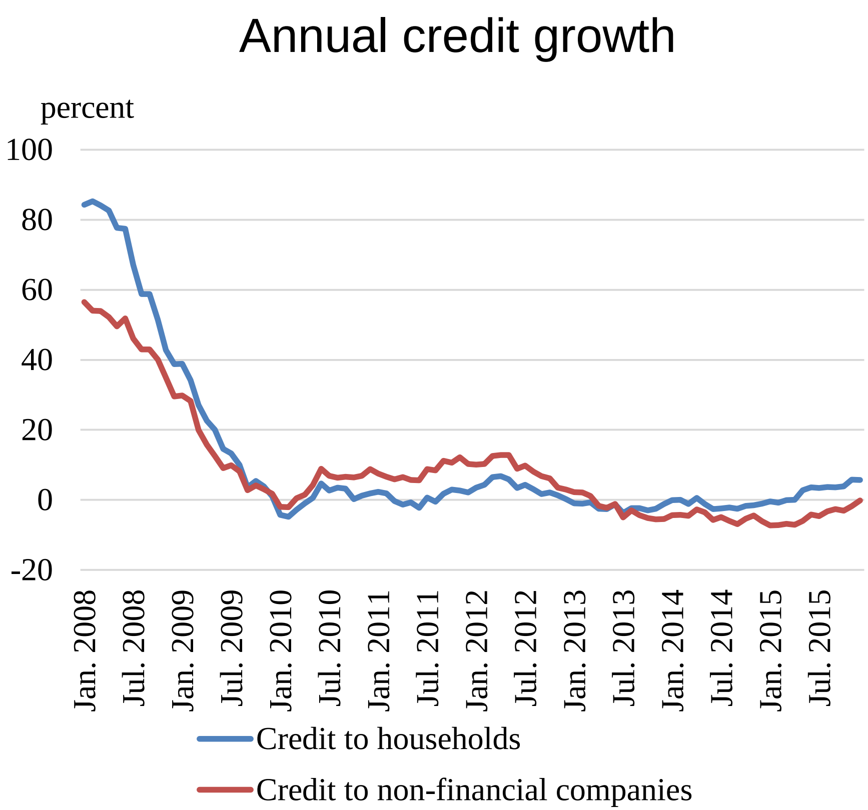


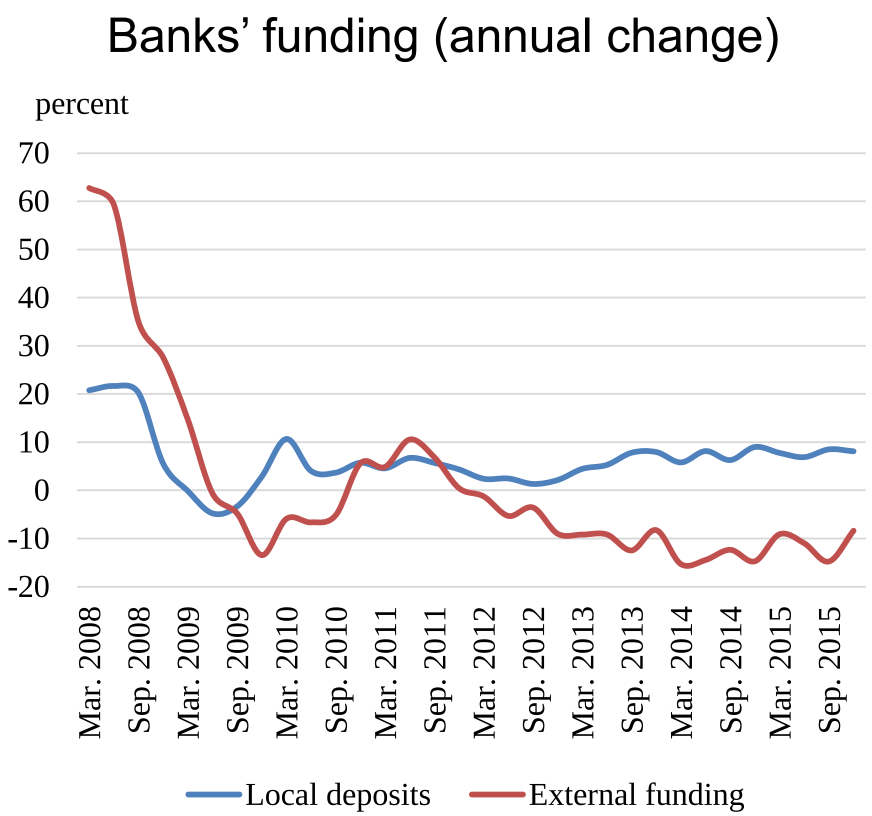


Source: NBR

Bank funding evolved toward lower contagion risk

- **Private sector credit resumed growth (households credit), but still feeble (creditless recovery?)**
- **Local deposits are replacing external funding; lower contagion risk**



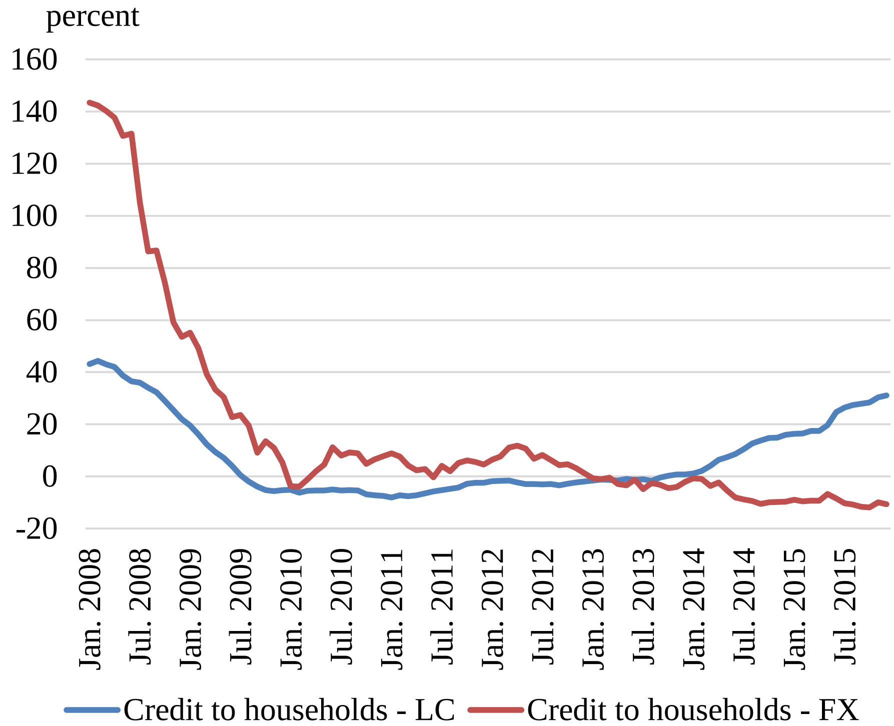


Source: NBR

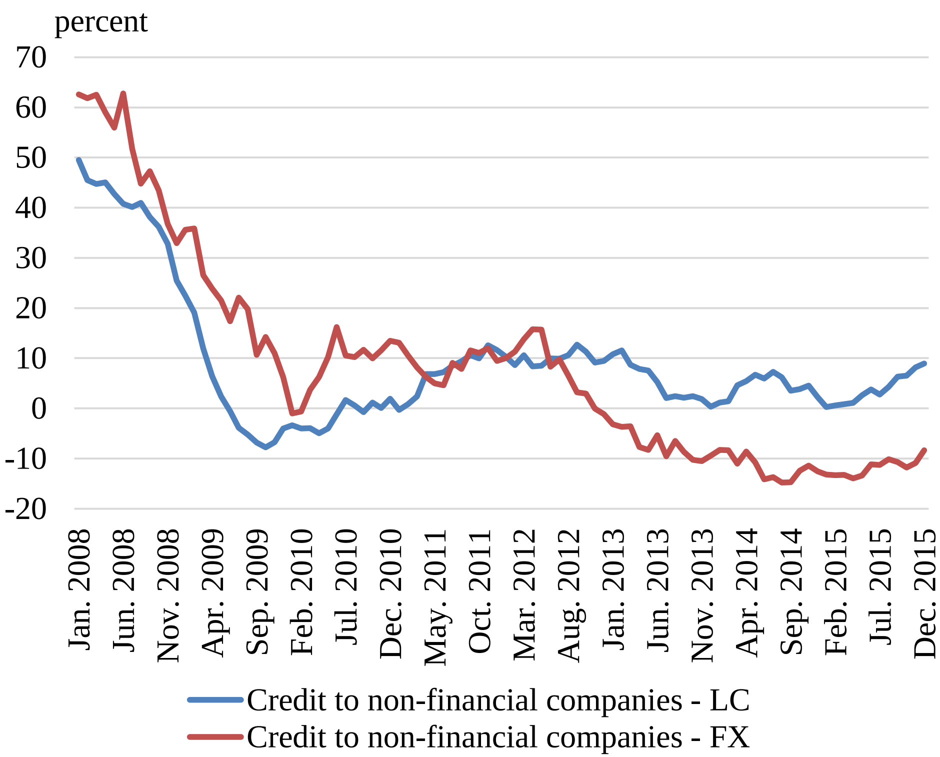
Credit growth in local currency resumed…

- **Local currency loans are the main driver of credit**
- ***Prima Casa* program counts for the largest share of new loans to households**

Credit to households (annual change)



Credit to non-financial companies (annual change)

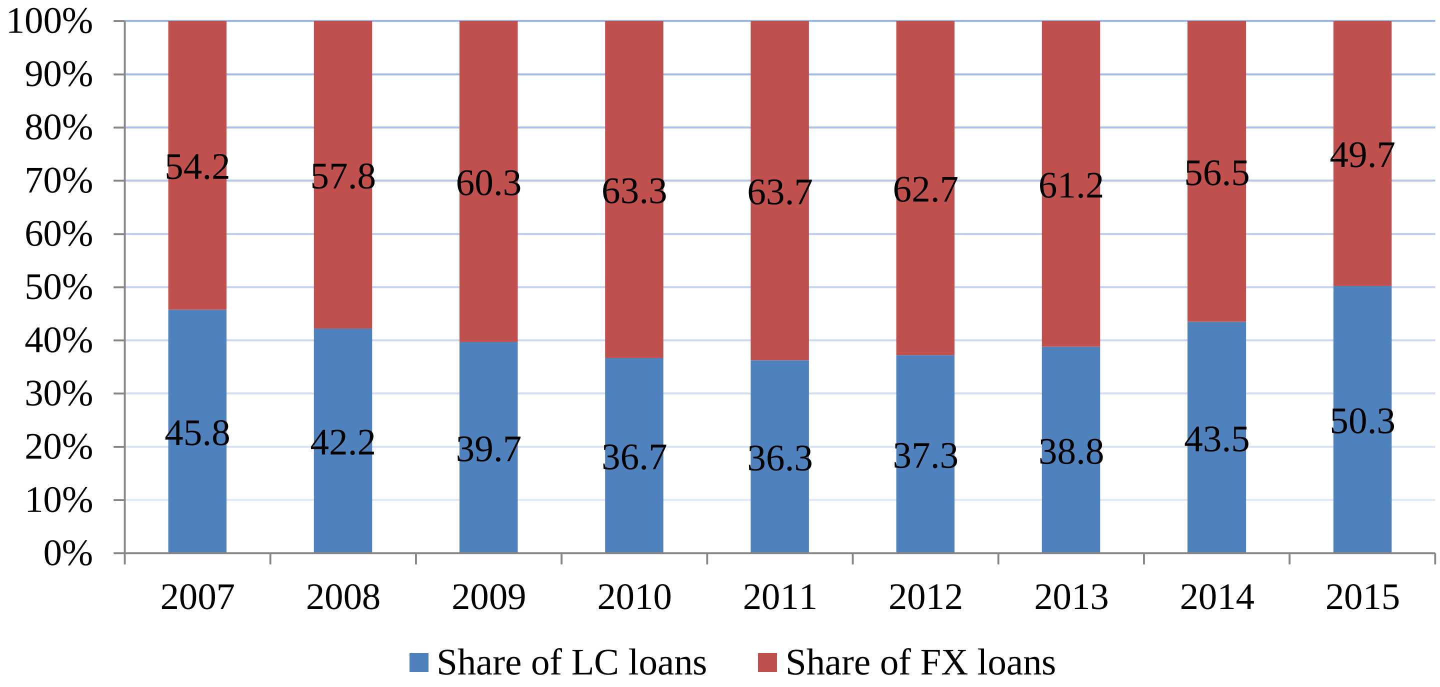


Source: NBR

… the majority of outstanding loans are local currency denominated now

- **In 2015 the share of local currency loans in banks' credit portfolios increased above 50%**
- **Banks' exposure to currency risk diminished since the onset of financial crisis**

Structure of banks' credit portfolios by currency (end of year)

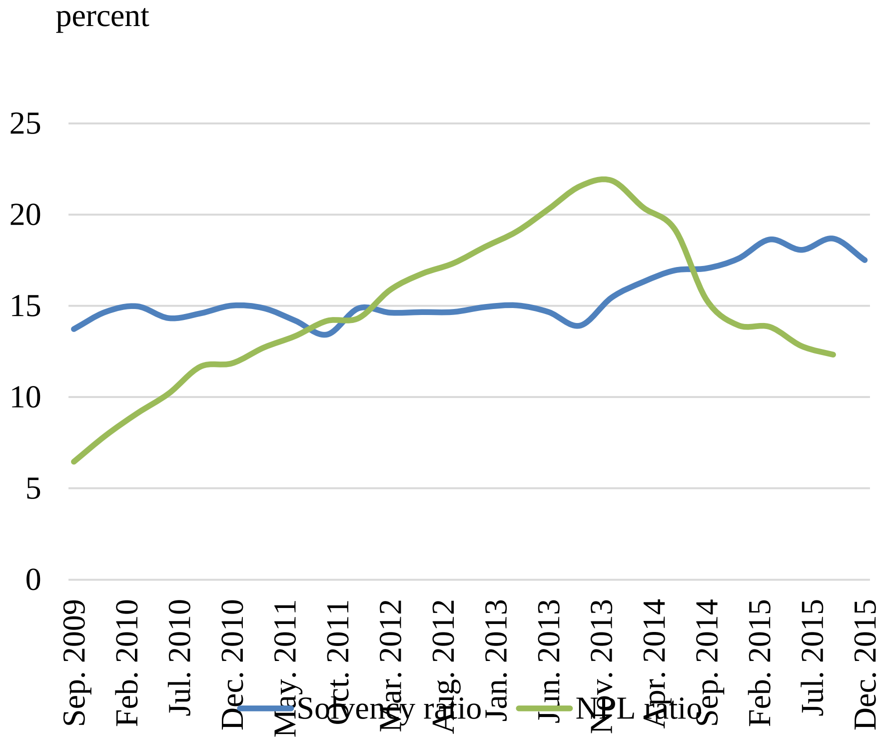


Source: NBR

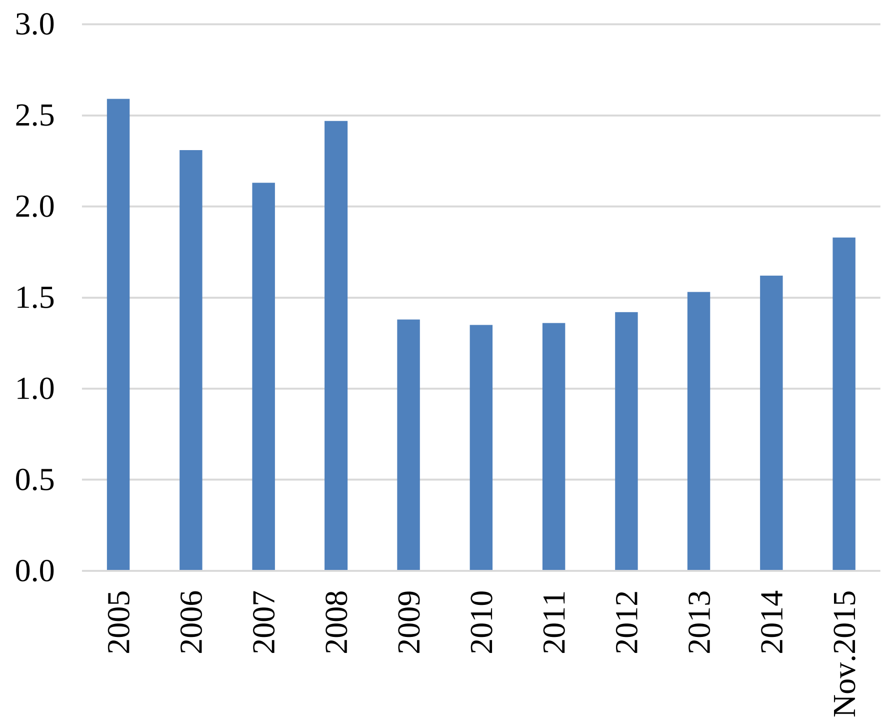
Banking sector improved its resilience to shocks

- **Banks' solvency and liquidity improved**
- **Banks have embarked on cleaning-up their balance sheets from bad loans**

Banks' solvency and NPL ratio



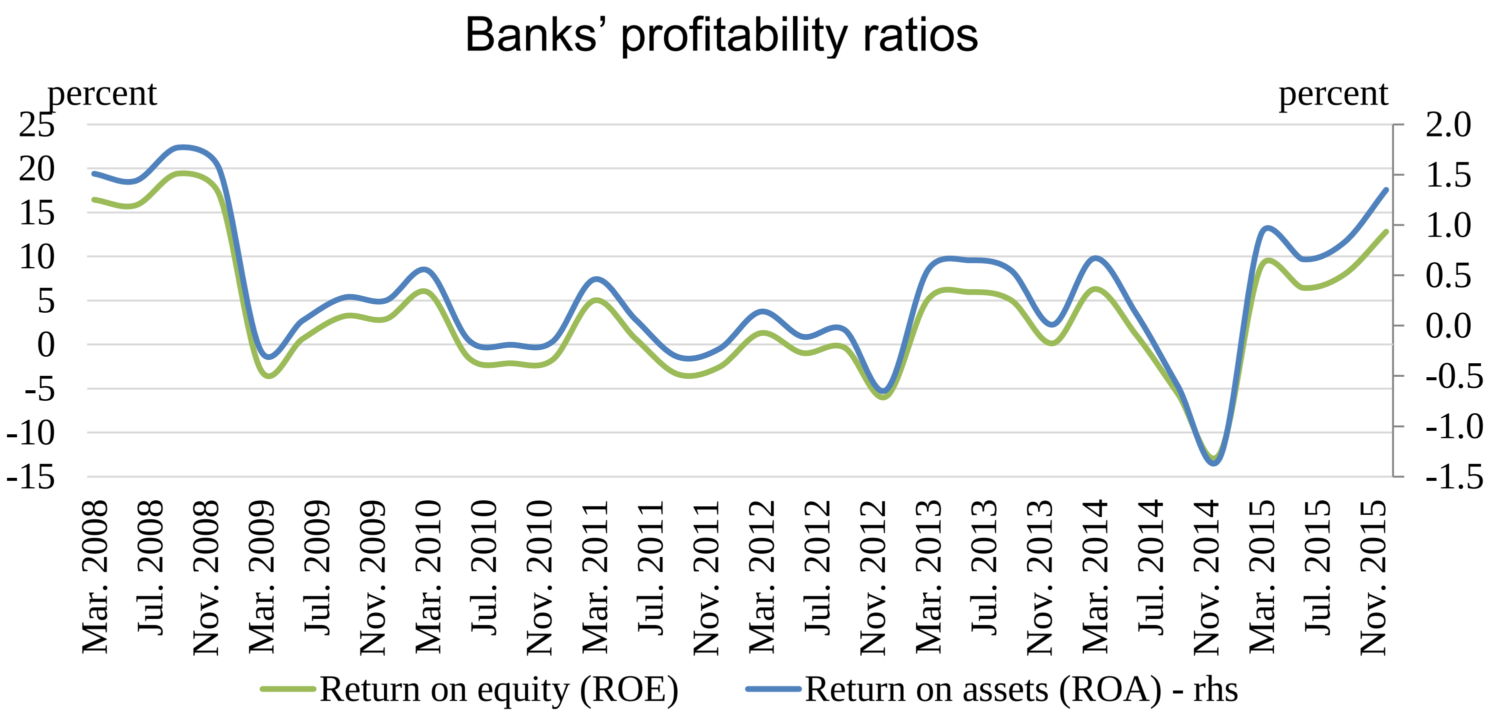
Liquidity indicator



Source: NBR

Banks' profitability went up in 2015

- Provision expenditures soared in the aftermath of the financial crisis
- Banks' profitability resumed growth in 2015 as bad loans were removed from balance sheets



Source: NBR

Banking sector's assets

Percent of total assets

	Dec. 2008	Dec. 2009	Dec. 2010	Dec. 2011	Dec. 2012	Dec. 2013	Dec. 2014	Dec. 2015
▪ Domestic assets, of which:	98	96.6	96.8	97.7	97.2	97	95.3	95.2
▪ Claims on the NBR and credit institutions, of which:	23.8	18.6	16.5	15.3	13.4	14.9	13.1	12.6
▪ Claims on the NBR	21.8	15.8	14.2	13.7	11.9	12.9	11.6	11.6
▪ Claims on the domestic non-bank sector, of which:	63.4	67.6	70.1	74.5	75.2	73.2	73.2	73.7
▪ Claims on the government sector	5	12.7	15.7	17.7	19.5	19.7	21.1	21.5
▪ Claims on companies*	29.2	27.4	27.9	30.3	30	28.2	26.9	26.3
▪ Claims on households	29.2	27.5	26.5	26.5	25.8	25.3	25.2	25.9
▪ Other assets	10.8	10.3	10.3	7.9	8.6	9	9	9
▪ Foreign assets	2	3.4	3.2	2.3	2.8	3	4.7	4.8

Note: Due to rounding, some totals may not correspond with the sum of the separate figures.

* Non-financial corporations and non-monetary financial institutions

Source: NBR – Aggregate monetary balance sheet data of credit institutions

Banking sector's liabilities

Percent of total liabilities

	Dec. 2008	Dec. 2009	Dec. 2010	Dec. 2011	Dec. 2012	Dec. 2013	Dec. 2014	Dec. 2015
▪ Domestic liabilities, of which:	69.3	73.6	73.2	73.5	76.8	79.5	82.3	84.5
▪ Interbank deposits	2.1	5.4	3.4	3.4	4.6	2.3	1.5	0.9
▪ Government sector deposits	3.1	2.1	1.7	1.4	1.3	1.3	1.5	1.6
▪ Corporate deposits*	20.2	19.3	19	19	18.5	21	23.5	25.6
▪ Household deposits	24.4	26.7	27	28.7	30.2	31.7	34.1	35.2
▪ Capital and reserves	10.6	12	14.2	16.2	18	19.4	18	17.5
▪ Other liabilities	8.9	8.1	7.9	4.8	4.2	3.8	3.8	3.8
▪ Foreign liabilities	30.7	26.4	26.8	26.5	23.2	20.5	17.7	15.5

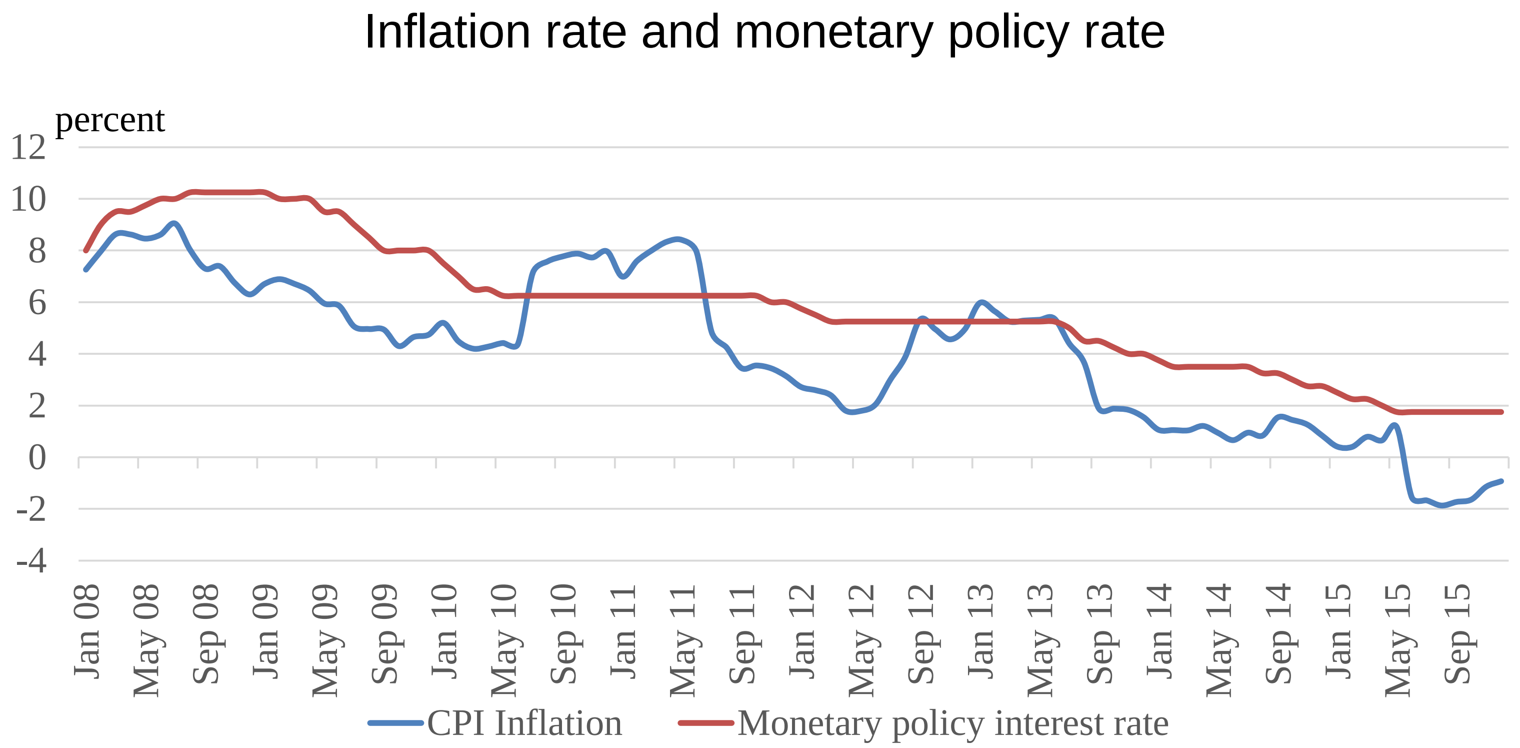
Note: Due to rounding, some totals may not correspond with the sum of the separate figures.

* Deposits from non-financial corporations and non-monetary financial institutions

Source: NBR – Aggregate monetary balance sheet data of credit institutions

Monetary policy rate declined drastically along with inflation

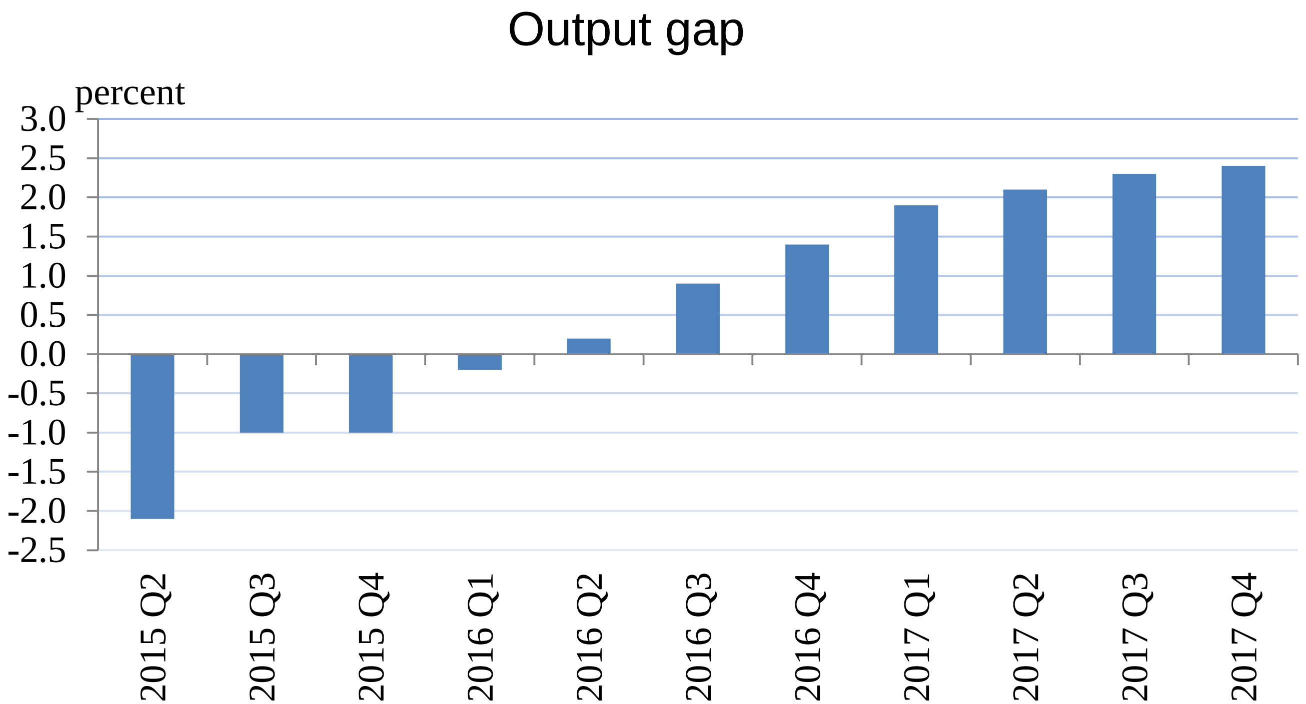
- Inflation rate has come down drastically over the past years
- Inflation rate has become negative due to VAT cuts; inflation is expected to return positive this year as the impact of tax cuts fades out



Source: NBR

Output gap is closing in

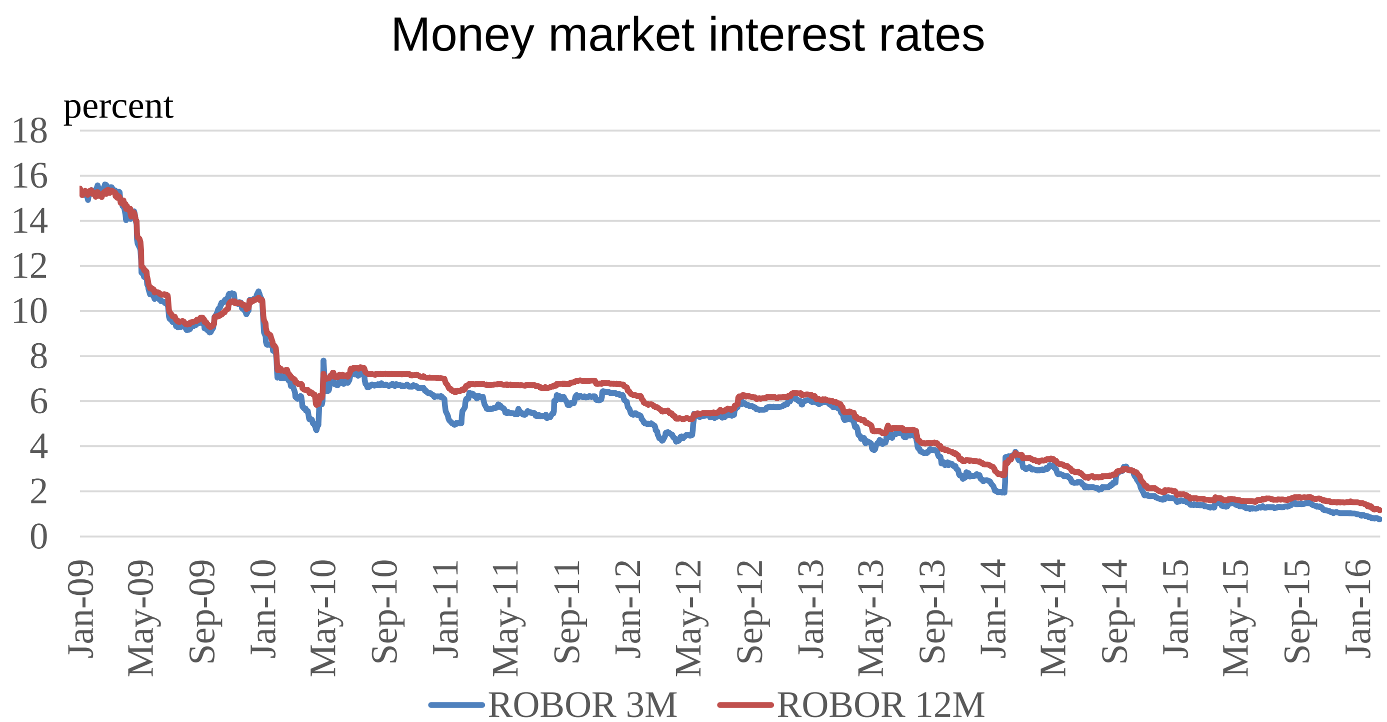
- Economic activity recovered the drop suffered during the crisis
- Export-led economic growth switched to consumption-led growth lately
- The output gap is expected to turn positive in the first half of this year



Source: NBR projections

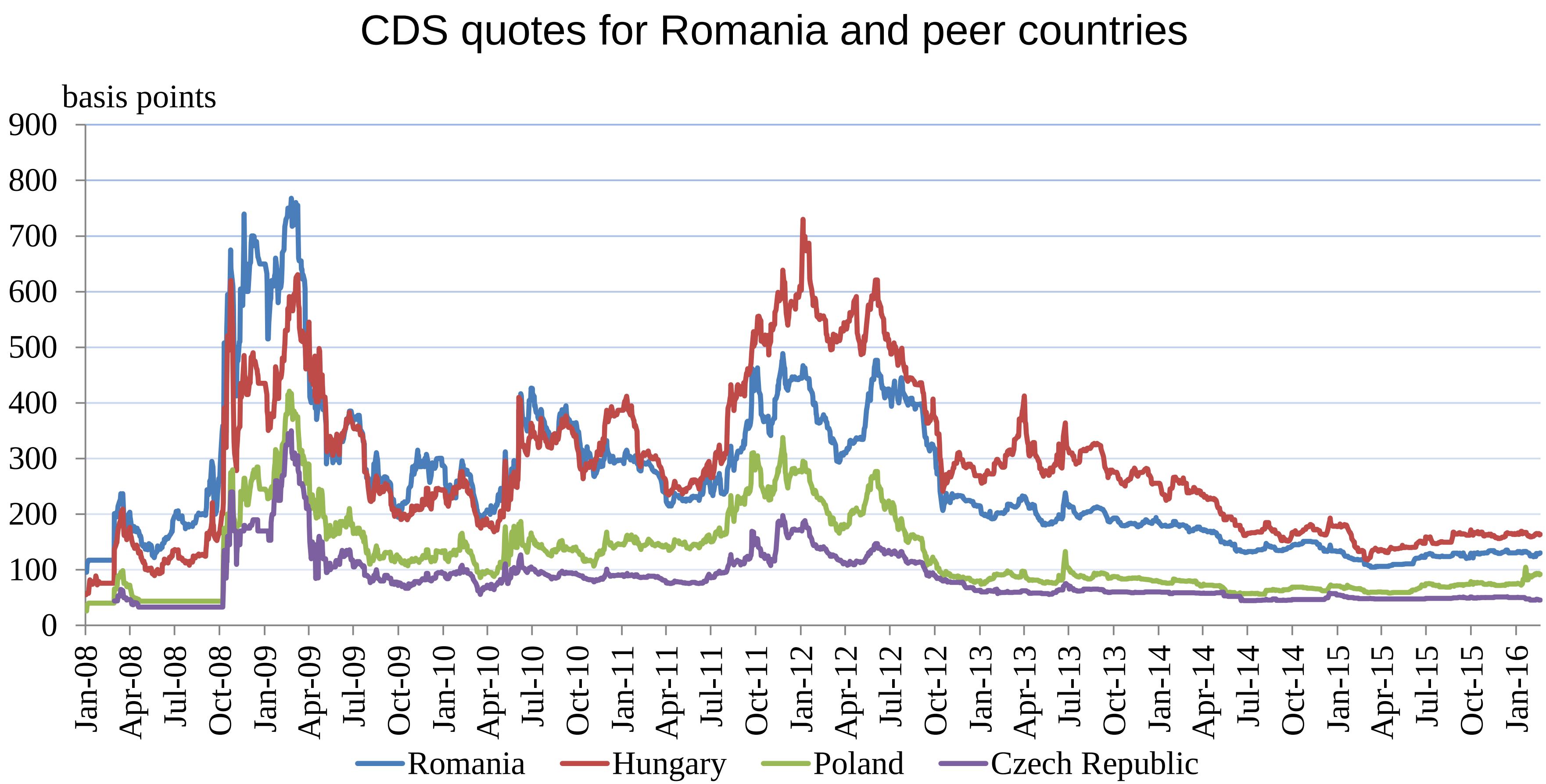
Credit costs at historical lows

- **Money market interest rates declined bellow 2 percent as NBR lowered significantly the monetary policy rate, while liquidity in the banking system is plentiful**
- **Low money market interest rates reduce costs for borrowers**



Source: NBR

Restored macroeconomic equilibria have improved investors' perception on country risk



Source: Reuters

Romania fulfills nominal convergence criteria, but more is at stake…

Maastricht Criteria
(Nominal Convergence Indicators)

Nominal Convergence Indicators	Maastricht Criteria	Romania	Fulfilment of the criteria
Inflation rate (HICP) (percent, annual average)	≤1.5 pp above -0.7% (average of the three best performing Member States*)	**-0.4** (December 2015)	Yes
Long-term interest rates (percent per annum, annual average)	≤2 pp above 1.9% (average of the three best performing Member States in terms of price stability*)	**3.5** (December 2015)	Yes
Exchange rate (vs. euro)** (percentage change)	±15 percent	**+1.8/ -1.8**	Yes
General government deficit*** (percent of GDP)	below 3 percent	**1.4**	Yes
Government debt*** (percent of GDP)	below 60 percent	**39.8**	Yes

*) Lithuania, Poland, Slovenia

**) Maximum percentage deviations of the bilateral exchange rate against the euro from its December 2013 average level in January 2014 to December 2015 based on daily data at business frequency. An upward/downward deviation implies that the currency was stronger/weaker than the average exchange rate in December 2013.

***) 2014; ESA2010 methodology.

Source: Eurostat

Romania as judged by rating agencies

- July 4, 2011 - Fitch Ratings raised the country’s sovereign rating to investment grade, with a stable outlook
- November 22, 2013 - Standard & Poor’s increased the outlook of Romania’s credit rating from stable to positive
- April 25, 2014 - Moody's Investors Service changed the outlook on Romania's government bond rating from negative to stable
- May 16, 2014 - Standard & Poor’s upgraded Romania to investment grade

Challenges ahead

External challenges

- Brexit, the refugees' crisis, sluggish economic growth in the euro area, and geopolitical risks increase uncertainty in a highly strained EU
- Policy divergence between the Fed and the ECB
- Fallout from emerging markets' crisis and worldwide economic slowdown
- Low commodity prices: assimetric consequences for companies, households and commodity producers

Domestic challenges

- Larger programmed budget deficits (budget pressures) weaken consolidation
- Legislative initiatives with an impact on banks and lending
- Bolstering public investment and setting priorities
- Furthering structural reforms; enhancing economic resilience