

panorama



Macroeconomic Report Romania 2013



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1. STRENGTHS AND CHALLENGES. COUNTRY RISK ASSESSMENT

Strengths	Challenges
<ul style="list-style-type: none"> Relatively large domestic market Significant foreign currency reserves Public indebtedness degree below the EU average 	<ul style="list-style-type: none"> Large exposure to the Euro zone Incompliant administrative and institutional sector Prone to political instability High indebtedness of the private sector Low level of governmental revenues as % GDP

Coface methodology concerning the country risk

Through country risk assessments, Coface measures the average risk of occurrence of payment incidents registered by companies from a certain country, thus promoting a higher focus on the business environment. Coface methodology considers (in the order of priorities):

- The payment experience of Coface, as insurer of commercial loans
- The business environment
- The economic and political prospects of the country

Coface maintained Romania's country risk assessment as B, the risk class that shows an unstable economic and political environment, able to impede an already scarce history of payments. Romania remains vulnerable due to the structural nature of internal and external unbalances and the high financing demand, in the context of insufficient domestic savings. The banking system remains affected by a higher level of bad loans.

2. SECTOR OF REAL ECONOMY. ECONOMIC GROWTH

According to the data published by NSI, the Gross Domestic Product related to Q3 of 2013 registered an increase by 4.1% (year-over-year) and by 1.6% (compared to the previous quarter). The increase registered during Q3, 2013 is the largest post-crisis and of the EU zone one (28).

↻ % Change compared to the previous quarter (series adjusted based on seasonal basis)

	Q1 - 2012	Q2 - 2012	Q3 - 2012	Q4 - 2012	Q1 - 2013	Q2 - 2013	Q3 - 2013
Romania	↓ -0.9%	↑ 1.5%	↓ -0.5%	↑ 1.1%	↑ 0.6%	↑ 0.5%	↑ 1.6%
EU	→ 0.0%	↓ -0.2%	↑ 0.1%	↓ -0.4%	↓ -0.1%	↑ 0.3%	↑ 0.1%
EU (17)	→ 0.0%	↓ -0.2%	↓ -0.1%	↓ -0.5%	↓ -0.2%	↑ 0.3%	↑ 0.2%

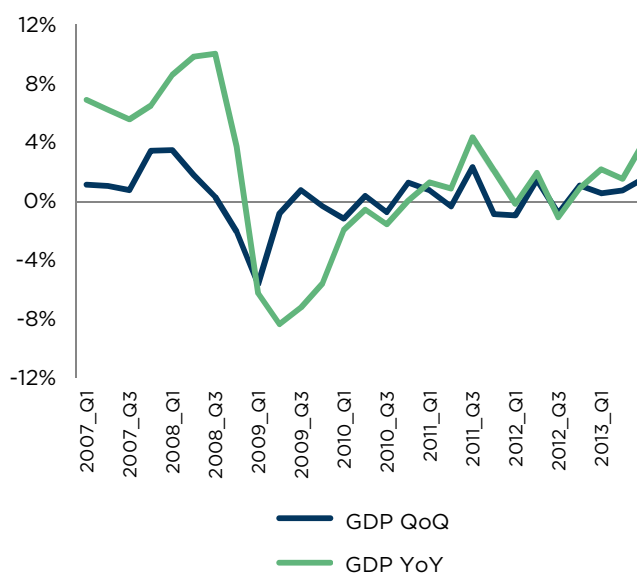
↻ % Change compared to the same quarter of the previous year (gross series, actual)

	Q1 - 2012	Q2 - 2012	Q3 - 2012	Q4 - 2012	Q1 - 2013	Q2 - 2013	Q3 - 2013
Romania	↑ 0.8%	↑ 1.8%	↓ -0.5%	↑ 1.2%	↑ 2.2%	↑ 1.5%	↑ 4.1%
EU	↑ 0.1%	↓ -0.3%	↓ -0.4%	↓ -0.7%	↓ -0.7%	↓ -0.1%	↑ 0.1%
EU (17)	↓ -0.1%	↓ -0.5%	↓ -0.6%	↓ -1.0%	↓ -1.2%	↓ -0.6%	↓ -0.4%
Romania among Top Economic Growths EU (28)				6th	3rd	5th	1st

For the entire term between January and September, 2013, Romania registered an actual GDP increase of 2.7%, supported by the following factors:

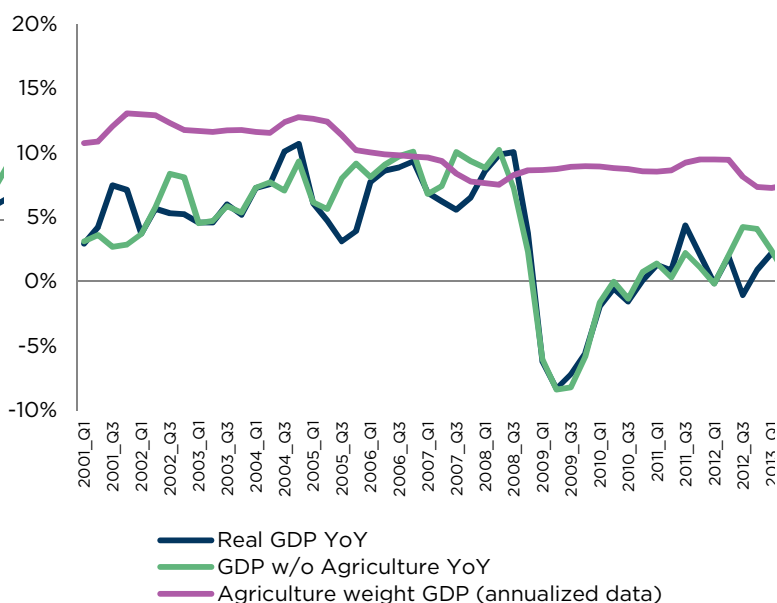
- The increase of exports of goods and services, which registered an increase by 12% (with a 9% increase of the export of goods), supported by the external demand from Germany (one of the main business and investment partners).
- The growth of industrial production, which registered an increase by 6.42% during the first 11 months of 2013, compared to the same period of time of the previous year, supported by the following export-oriented industrial sectors:
 - Transportation machines and equipment, which generate 24% of the overall exports performed during the first 10 months of 2013, and which registered an 11% increase compared to the same period of time of the previous year.
 - Raw materials, which registered a 9% increase of exports during the first 10 months of 2013.
 - The food and beverage industry, which registered a 16% increase of exports during the first 10 months of 2013.
- The growth of agricultural production, which registered a 25% increase during 2013, according to the data published by Eurostat. Whereas a significant part of the agricultural production is obtained based on self-management activities (with no lucrative purpose), the agricultural sector is affected by low productivity, and the results are highly dependent on the weather conditions. Whereas agriculture generates approximately 6% of the GDP, the results of this sector can significantly influence the GDP increase, generating a high volatility, poor and little predictable sustainability. As we can see in Fig. no. 2, by removing the positive impact of agriculture in the GDP, we can notice the following:
 - The actual increase registered in 2012 would have been of 2.5%, compared to the only 0.6% actually registered one, whereas agriculture had a negative impact on the GDP (-2pp).
 - The actual economic growth of the first 9 months of 2013, compared to the previous year, would have been of only 1.5%, compared to 2.7%.
 - Thus, we can notice 2 consecutive years (2012 & 2013) that registered extremely different growths (0.6%, and 2.5%, according to Coface annualized estimates), but that look completely different (with 2012 better than 2013) if we adjust the effect of agriculture (2.5% adjusted increase in 2012, compared to 1.5% adjusted increase in 2013).

Fig. 1 - Evolution of quarterly GDP



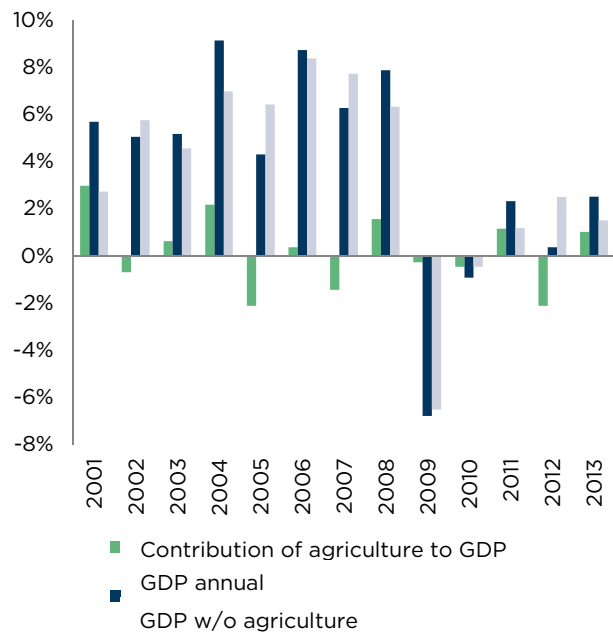
Source: NSI, data processed by Coface

Fig. 2 - Quarterly GDP (with and without agriculture)



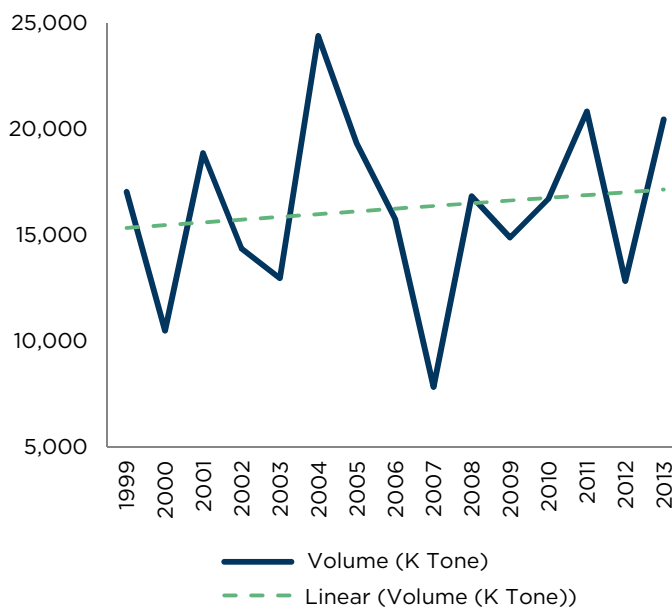
Source: NSI, data processed by Coface

Fig. 3 - Annual GDP evolution (with/ without agriculture)



Source: NSI, data processed by Coface

Fig. 4 - Production of grains



Source: NSI, data processed by Coface

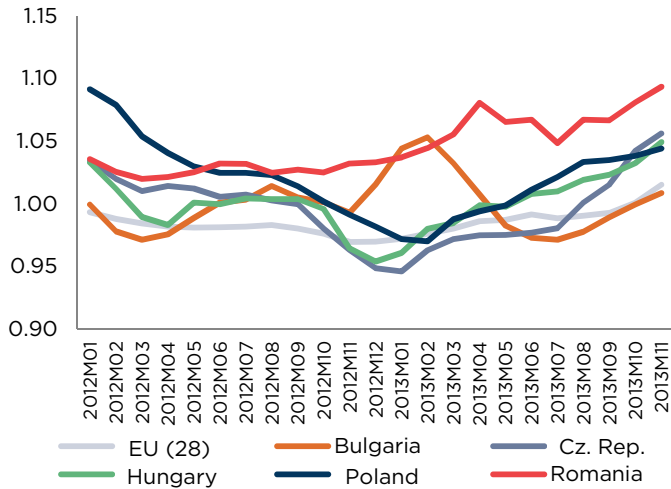
With respect to the short-term evolution of indicators compared to the EU zone (28), we can notice the following:

- Compared to the previous year, during the first 11 months of 2013, the Romanian industrial production registered an average increase by 6.42% (according to Eurostat). As we can see in Figure 5, this is the highest growth registered in the EU zone (28). Furthermore, industrial production is the only Romanian sector that has registered a constant growth during the last 2 years, at a constant pace. Thus, during the entire term between 2012 and 2013, Romania registered the highest increase of the EU zone (28) on industrial production (the only exceptions being Poland, with a higher increase in Q1 2012, and Bulgaria in Q1, 2013). Also, according to the opinion questionnaires reported by Eurostat, the level of confidence in industry registered by Romanian economic operators is at a comparable level with the one registered in the EU zone (28) and far above the one registered in Poland (Fig. 6).

- Compared to the previous year, during the first 11 months of 2013, the volume of construction works performed in Romania registered an average decrease by 1.7% (according to Eurostat). As we can see in Fig. 7, the construction works registered a strong recovery during July and September, which compensated for the significant decrease of the first half of the year (-7% year-over-year, seasonally adjusted series). The dynamics of construction works in Romania was somehow in line with the evolution in the EU zone (28), where only two countries (Spain and Hungary) registered a slight increase of this indicator, while other countries registered decreases by more than 10% (Czech Republic, Italy, Poland and Portugal). According to the opinion questionnaires reported by Eurostat, the level of confidence in construction industry registered by Romanian economic operators is at a comparable level with the one registered in the EU zone (28) and far above the one registered in Poland and the Czech Republic (Fig. 8).

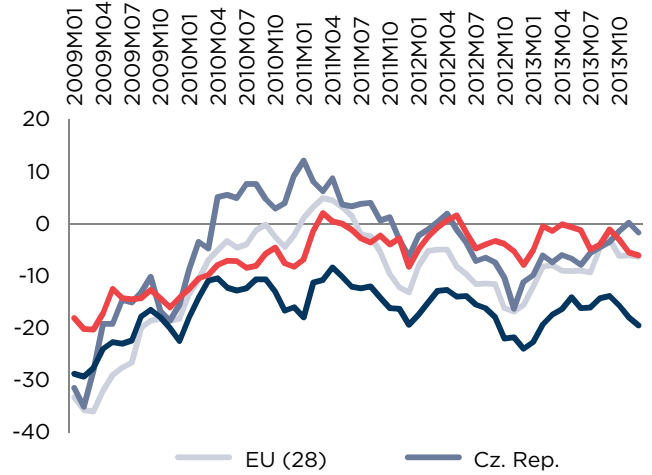
- Compared to the previous year, during the first 11 months of 2013, Romanian retail trade registered an almost stagnant evolution, with only 0.1% turnover related to this sector during the analyzed period of time. As we can see in Fig. 9, the evolution of this sector during 2013 was also extremely modest for the EU zone (28), which registered an average stagnation. However, there are countries like Lithuania, Latvia or Poland, which registered increases of more than 5%, while at the opposite side, Spain, Serbia or Greece registered decreases by more than 5%. According to the opinion questionnaires reported by Eurostat, the level of consumer confidence registered by Romanian economic operators is lower than the one registered in the EU zone (28) and far below the one registered in Poland and the Czech Republic (Fig. 10).

Fig. 5 - Industrial Production (% of the previous year, 3M mobile average)



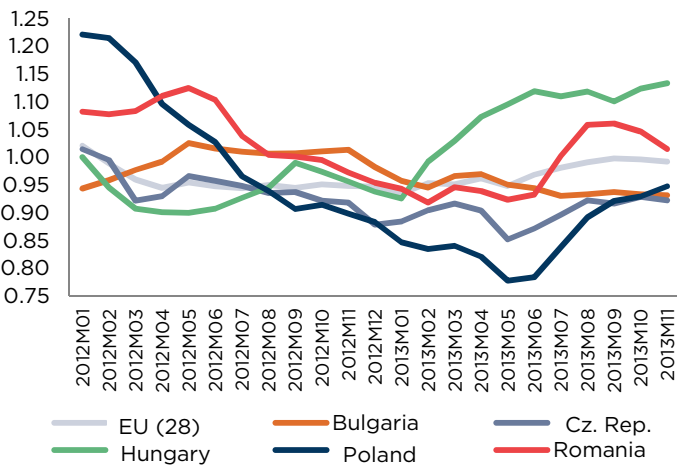
Source: Eurostat, data processed by Coface

Fig. 6 - Level of confidence in the industry



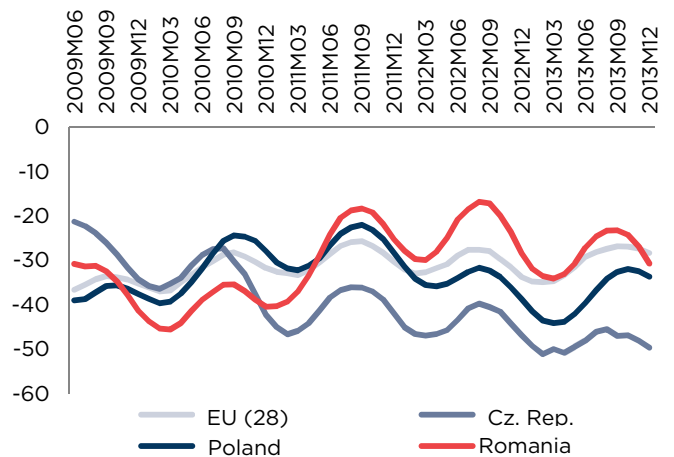
Source: Eurostat, data processed by Coface

Fig. 7 - Volume of construction works (% of the previous year, 3M mobile average)



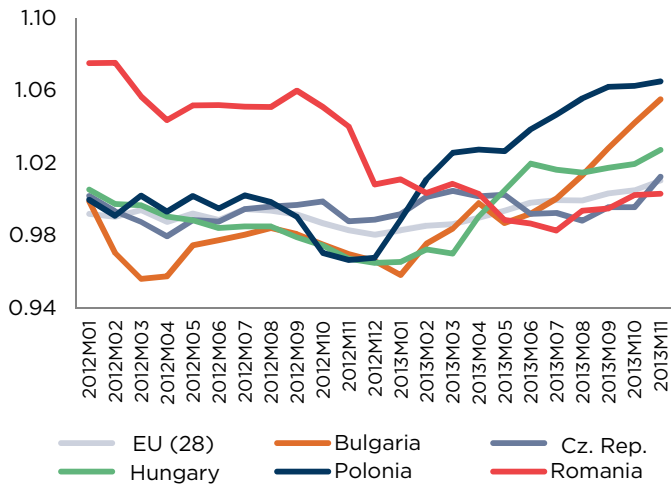
Source: Eurostat, data processed by Coface

Fig. 8 - Level of confidence in constructions



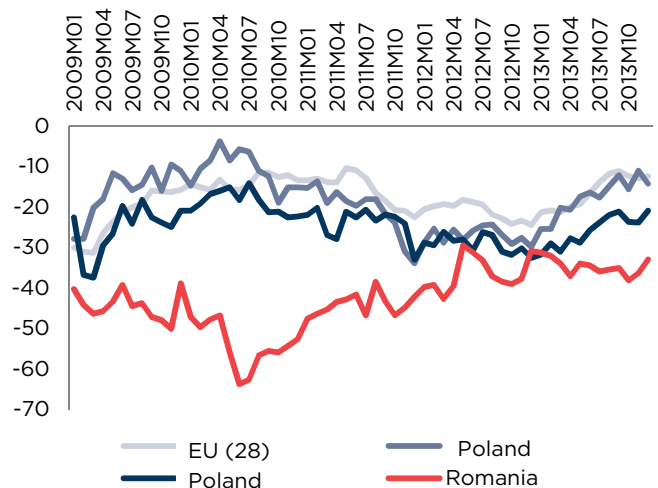
Source: Eurostat, data processed by Coface

Fig. 9 - Volume of construction works (% of the previous year, 3M mobile average)



Source: Eurostat, data processed by Coface

Fig. 10 - Level of consumer confidence



Source: Eurostat, data processed by Coface

The data available on short-term indicators shows that local economy had a promising start in Q4. The construction's volume increased by 7.4% in October and by 4.4% in November (year-over-year). Industrial production also increased by 10% in October and November (year-over-year). Thus, in the basic scenario for 2013, we estimate that the annual GDP increase amounts to at least 2.5%, the final figures depending on the forecasted decreasing level of consumption in December.

For 2014 we expect for the economic business to maintain its ascending trend, but with a slightly moderate final growth, in the context of:

- A more moderate increase of exports compared to 2013 - in addition to the registration of a significant increase for 2013 and which shows a significant basic effect, the main contribution of increased exports came from the area of transportation machines and equipment industry, which is hard to repeat in the next year. Thus, in the basic scenario we expect an increase of exports by maximum 5% during 2014.
- A zero contribution of agriculture to the economic growth - even though during the last 10 years agriculture registered a sinusoidal evolution, by generally alternating better and weaker years of agricultural production, the probability of extreme shocks from this area is low.
- The gradual but hard recovery of consumption - even though there are voices that consider consumption as the main growth booster for the next year (the main arguments consisting of the marginal increase of the available income, based on the increase of the national minimum wage, the generally low loan-related costs, and in particular in the local currency, the low inflation prospects during the first half of the year), we appreciate that the consumption increase will not be a spectacular one (maximum 2% year-over-year for 2014), because:
 - Tax policies with additional taxes, with no survey on the precise impact on available revenue
 - Accelerated inflation during the second half of the year
 - The extremely low confidence of domestic consumers and orientation thereof towards saving and indebtedness-free, as shown by the data on financial disintermediation hereof.
- On the contrary, industrial production shall benefit from the increase of exports, as this sector is the main candidate for the most important growth supporting factor for the year to come.

Under these circumstances and in the context of side slips on the political stage, we expect an actual GDP increase of 2.1% for 2014 (basis scenario), which is anyway a better result, compared to the one registered in 2013, eliminating the effect of agriculture (approximately 1.5%).

3. BALANCE OF PAYMENTS AND THE INVESTMENT POSITIONING

The current account deficit registered between January and November, 2013 was of 1.32 BEUR, a significant recovery compared to the level registered during the same period of time of the previous year, namely 5.4 BEUR. The main factor that supported these dynamics was the contraction of the commercial deficit, which during the analyzed term decreased from -5.7 BEUR to -0.65 BEUR, in the context of increased export of goods and services (+12%), which significantly exceeded the dynamics of imports (1%). The modest domestic demand and the decrease of investments in the gross generation of capital (-4% January - September year-over-year) reflected the extremely low evolution of imports, in particular of fuel imports (in the context of favorable weather conditions).

MEUR (Balance)	2012 - Q1	2012 - Q2	2012 - Q3	2012 - Q4	2013 - Q1	2013 - Q2	2013 - Q3*
Current Account Deficit	- 1,031	- 3,152	- 4,800	- 5,843	75	241	- 616
Commercial Deficit	- 1,139	- 3,215	- 4,905	- 6,249	39	- 225	- 570
Exports	12,834	26,231	39,482	53,472	13,918	28,766	44,360
Imports	13,973	29,446	44,387	59,721	13,879	28,991	44,930
Foreign Direct Investments	353	751	1,662	2,139	414	1,262	1,277
(% Same period previous year)	2012 - Q1	2012 - Q2	2012 - Q3	2012 - Q4	2013 - Q1	2013 - Q2	2013 - Q3*
Current Account Deficit	↑ 76.56%	↓ -5.50%	↑ 0.74%	↓ -1.37%	↓ -107.24%	↓ -107.66%	↓ -87.17%
Commercial Deficit	↑ 24.33%	↓ -2.69%	↓ -4.92%	↓ -11.41%	↓ -103.42%	↓ -93.00%	↓ -88.38%
Exports	↑ 2.16%	↑ 3.05%	↑ 1.61%	↑ 1.76%	↑ 8.45%	↑ 9.66%	↑ 12.35%
Imports	↑ 3.66%	↑ 2.39%	↑ 0.84%	↑ 0.20%	↓ -0.67%	↓ -1.55%	↑ 1.22%
Foreign Direct Investments	↑ 108.42%	↑ 58.19%	↑ 93.10%	↑ 17.89%	↑ 17.43%	↑ 67.93%	↓ -23.15%

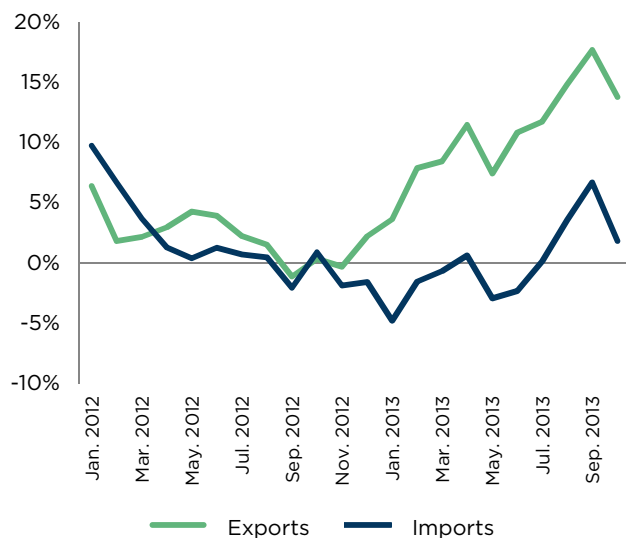
Balance figures, at the end of the analyzed period, expressed in MEUR

* Preliminary data

Thus, the current account deficit of 2013 will most likely range around -1.3% of the GDP, following to reach 2% for 2014. The slight depression of the current account deficit shall register in the context of export deceleration and a more sustained increase of imports, in the context of a gradual recovery of the local demand.

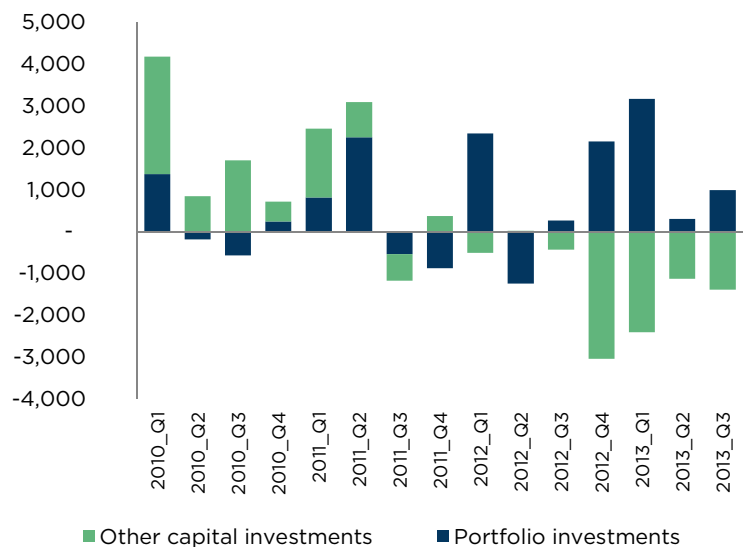
The foreign direct investments (FDI) cumulated for January - November, 2013 amounted to 2.38 BEUR, by approximately 22.3% higher than during the same period of time of the previous year. The growth in the analyzed period is due strictly to the positive evolution in November, when capital inflows of 496 MEUR were registered. Except for November, for instance, FDI registered a decrease of approximately 4% in the period January-October 2013/2012. Out of the total FDI, approximately 82% came from the EU zone (28), showing a decreasing trend compared to 2011 - 2012, when the weight was of more than 90%. Thus, while Austria, France and Germany generated 80% of the direct foreign investments in Romania in 2012, in 2013 these cumulated a weight of only 50%, in the detriment of other EU countries (such as Spain or Hungary) or extra-community countries (USA and Switzerland, for instance, generated approximately 15% of the FDI during 2013). Under these circumstances, FDI will most likely cumulate approximately 2.5 BEUR for the entire 2013, and around 2.5 - 3 BEUR during 2014.

Fig. 11 - Exports vs. Imports (3M mobile amount, % year-over-year)



Source: NBR, data processed by Coface

Fig. 12 - Net Inflow - Foreign Private Capital (MLN EUR)



Source: NBR, data processed by Coface

By analyzing the structure of private capital inflows in the balance of payments, we can notice the increasing contribution of portfolio investments, which can record a higher volatility. The overall level of portfolio investments related to January - November, 2013 amounted to 3.88 BEUR, by 51% higher compared to the same period of time of the previous year, when 2.57 BEUR inflows were registered. November generated a significant impact in the annual evolution of portfolio investments, i.e. 757 MEUR capital outflows in November 2013, and 1.3 BEUR inflows in November 2012. Thus, by analyzing the dynamics of portfolio investments for the period January - October, we note that the growth is approximately 220%. The negative events registered on the international stage during June - August weakened the confidence in emerging markets, and Romania lost approximately 1 BEUR of portfolio investments during the said period of time. The balance figures of portfolio investments related to the last 3 years show a high volatility, which generates the non-sustainability and the lack of predictability concerning the current account deficit.

4. MONETARY POLICY, FINANCIAL MARKETS AND T-BONDS

The overall average increase of prices, during the last 12 months (January, 2013 - December, 2013) compared to the previous 12 months (January, 2012 - December, 2012), determined based on CPI, was of 4%. The evolution of inflation during 2013 registered two different stages during the two semesters. Thus:

- During the first half of 2013 the annual inflation ranged between 5% and 6% (year-over-year), in the context of the basic unfavorable effect (decrease during the first half of 2012) and increase of electricity price by 6%, as well as of the price of excisable products in the context of higher exchange rate (from 4.30 to 4.52) based on which the excise taxes were determined for 2013
- Q3 was marked, for the first time during the last years, by the decrease of prices (disinflation) and the end of H2 registered the minimum historical level of annual inflation, in the context of:

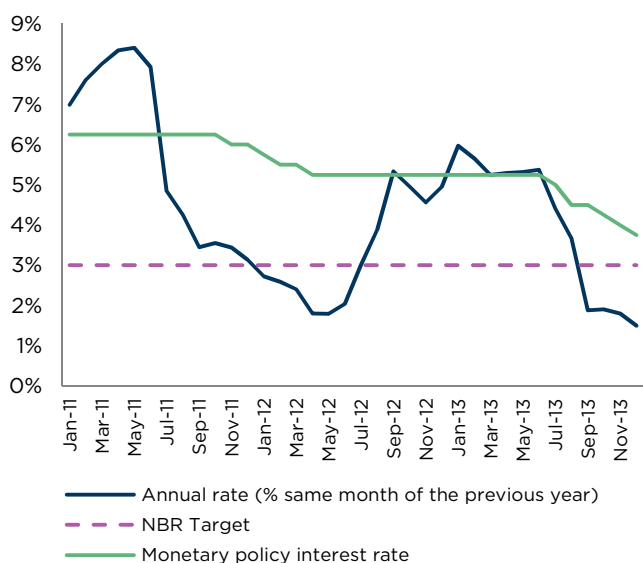
- The decrease of VAT for bread-related products from 24% to 9% as of September 1, which will convey a decreasing effect of the annual inflation by the end of August, 2014
- The favorable basic effect in the context of an extremely good 2013 agricultural year, so that the prices of volatile products decreased

Under the circumstances of delayed implementation of the fuel-related excise tax until Q2 of 2014, we expect that the inflation related to the first three months of the current year shall not exceed 1%. The inflationist pressures will increase towards the end of the year, so that the annualized inflation related to the entire 2014 shall reach 3% - 3.5% (higher level of the floating band concerning the NBR inflation target), being fueled by:

- The activation of fuel-related excise tax
- The loss of the basic effect related to the VAT decrease for bread-related products
- The gradual recovery of consumption
- The European parliament and presidential elections of the second half of the year, which will probably determine higher populist governmental expenses

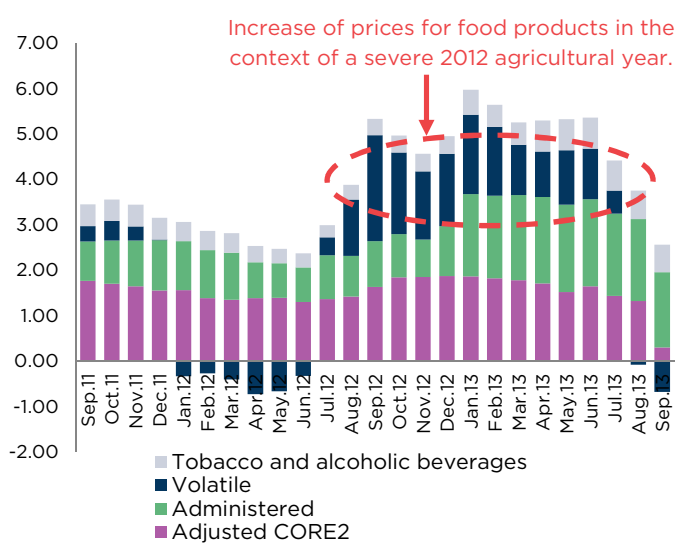
A more relevant indicator for medium-term inflation can be obtained by excluding the effect of volatile prices (fruits, vegetables, eggs and fuel). Thus, during 2013 the level of adjusted CORE 2 inflation ranged between 0.3% and 1.5% (Fig. 14)

Fig. 13 - Evolution of inflation



Source: NBR, data processed by Coface

Fig. 14 - Annual inflation - contributions per components



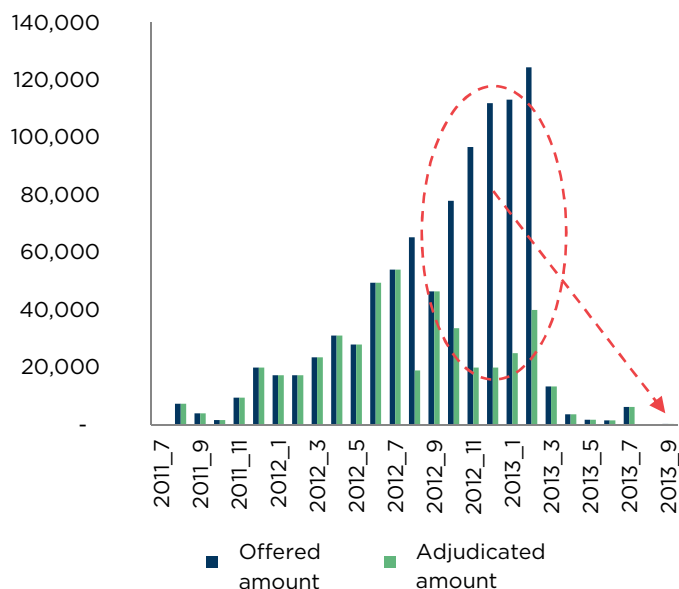
Source: NBR, data processed by Coface

The interest rates of the inter-banking market significantly decreased for all maturities, in the context of the massive portfolio investments registered at the beginning of 2013 (3.1 BEUR, almost equal with the level registered in 2012), fueled by the inclusion of Romanian T-bonds in the Barclays and JP Morgan index at the beginning of 2013. Thus, the ROBOR rates for 1 month decreased from 6%, level registered at the beginning of 2013, to almost 2% at the end of the same year, and in the middle of January, 2014 decreased to 1.41%. The levels of ROBOR 6, 9 and 12 months, became extremely similar, ranging between 2.6% - 3.3% at the beginning of 2014, compared to a floating range of 6%-7% during the same period of time of the previous year. The moment when the disinflation prospects of the beginning of H2 of 2013 became obvious, the NBR decreased the monetary policy interest by 150 bp (basis points) between June and December, 2013, by means of four consecutive

decreases. Thus, the liquidity surplus significantly increased in November and December, in the context of increased public expenditures financed through the issuance of bonds denominated in EUR. Despite this fact, NBR was forced to initiate sterilizing actions against the liquidity surplus, because the investors maintained positive feelings regarding the T-bonds. The monetary policy interest may be decreased to 3.5% by the end of Q1 of the current year, and decreases of the level of minimum mandatory reserves are not excluded. Despite this fact, the inflationist pressure forecasted for the second half of the current year will most likely moderate the monetary relaxation measures of the central bank.

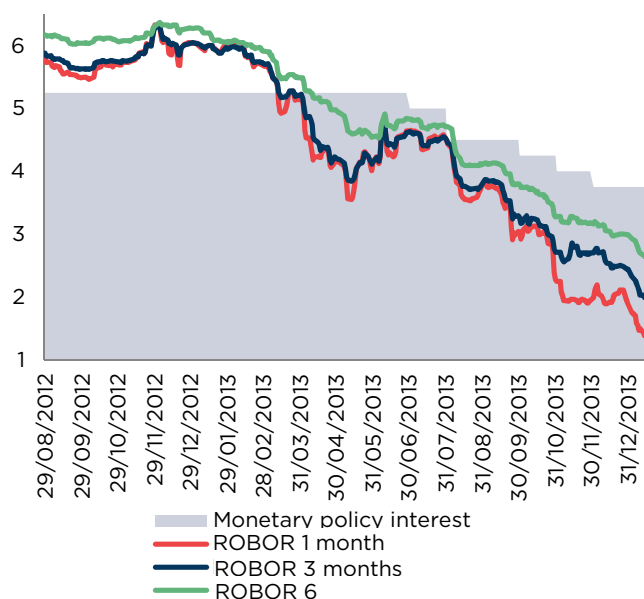
The entire context of the above mentioned monetary policy should have, at least in theory, a favorable effect on the re-launching prospects of economic growth financing and support. This can already be seen, at least with respect to the orientation of new loans towards the local currency, with a weight that increased from 35% (balance registered at the beginning of 2012) to 39% (balance registered in November, 2013). Despite this fact, as we will see in the last chapter (Financial brokering) of this report, the credit-related appetite of the private environment is extremely low, both on the corporate and on the retail segment.

Fig. 15 - Repo Transactions (MLN RON)



Source: NBR, data processed by Coface

Fig. 16 - Interest rates - inter-banking monetary market



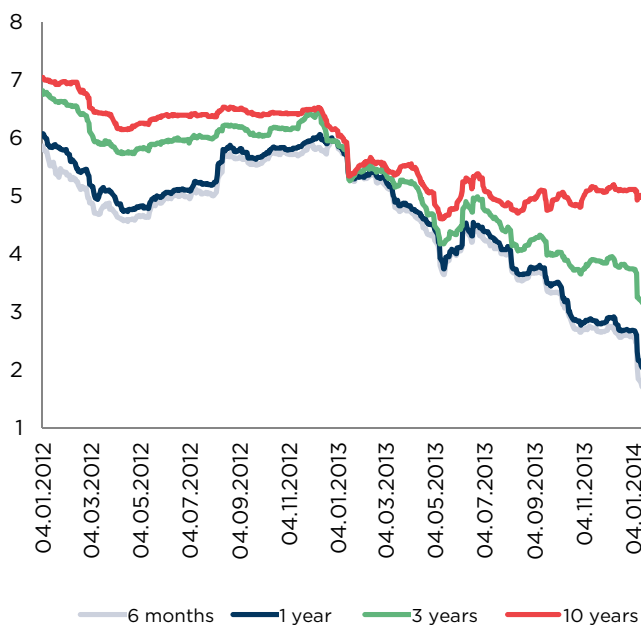
Source: NBR, data processed by Coface

The investors' interest for T-bonds denominated in RON changed radically between 2012 and 2013. During March - November, 2012, these registered a contraction of 5 BRON, in the context of political tensions and side slips, and generated significant pressure on the depreciation of local currency. The political stability and inclusion of Romanian T-bonds in Barclays and JP Morgan index for the emerging markets determined the increase of the volume of T-bonds denominated in RON, by non-residents, by approximately 14 BRON during December, 2013 - February, 2014. The concerns related to the moderation of the pace in which FED acquires financial assets (tapering) determined capital outflows of approximately 2.4 BRON during May - October (decrease from 21.6 BRON to 19.2 BRON). Despite these turbulences, the balance of the volume of T-bonds denominated in RON, held by non-residents, increased during January - October, 2013 by approximately 9 BRON, and the weight thereof in the overall T-bonds denominated in the local currency increased from 5% (percentage registered in balance in November, 2012) up to approximately 22% (percentage registered in balance in October, 2013).

The interest rates related to T-bonds showed a trend in line with the dynamics of the inter-banking monetary market, with a higher contraction for the first part of the yield curve, and determined the deepening thereof (“steepening yield curve”, fixing ask price). The public debt stabilized during the last two years to 38.2% of the GDP, and most likely will maintain the same level for the current year, in the context of a liquidity buffer accumulated by the Ministry of Finance.

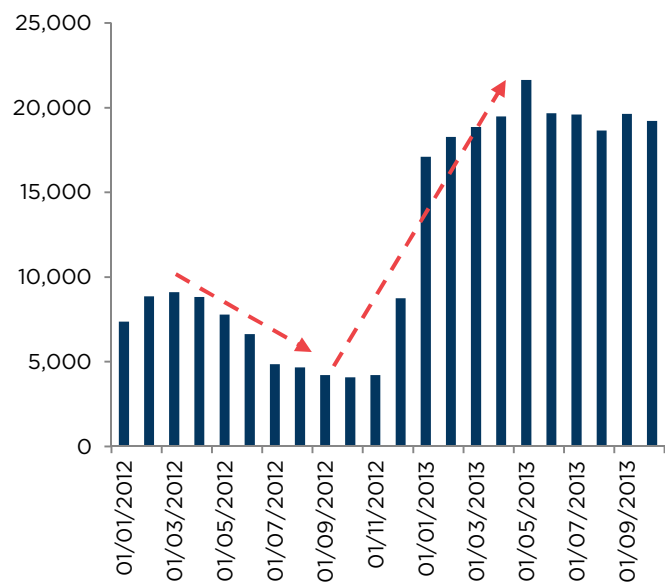
Despite the reimbursement of approximately 5 BRON of the loan contracted from the IMF, the foreign currency reserves of the NBR increased by approximately 4%, to 32.4 BRON (November, 2013), and cover more than 7 months of imports. Thus, the level is sufficient in order to accommodate the next reimbursement installment related to the IMF loan, of 4.7 BRON, during 2014.

Fig. 17 - T-bonds - Fixing (ASK Prices %)



Source: NBR, data processed by Coface

Fig. 18 - T-bonds denominated in RON (held by non-residents, MRON)



Source: NBR, data processed by Coface

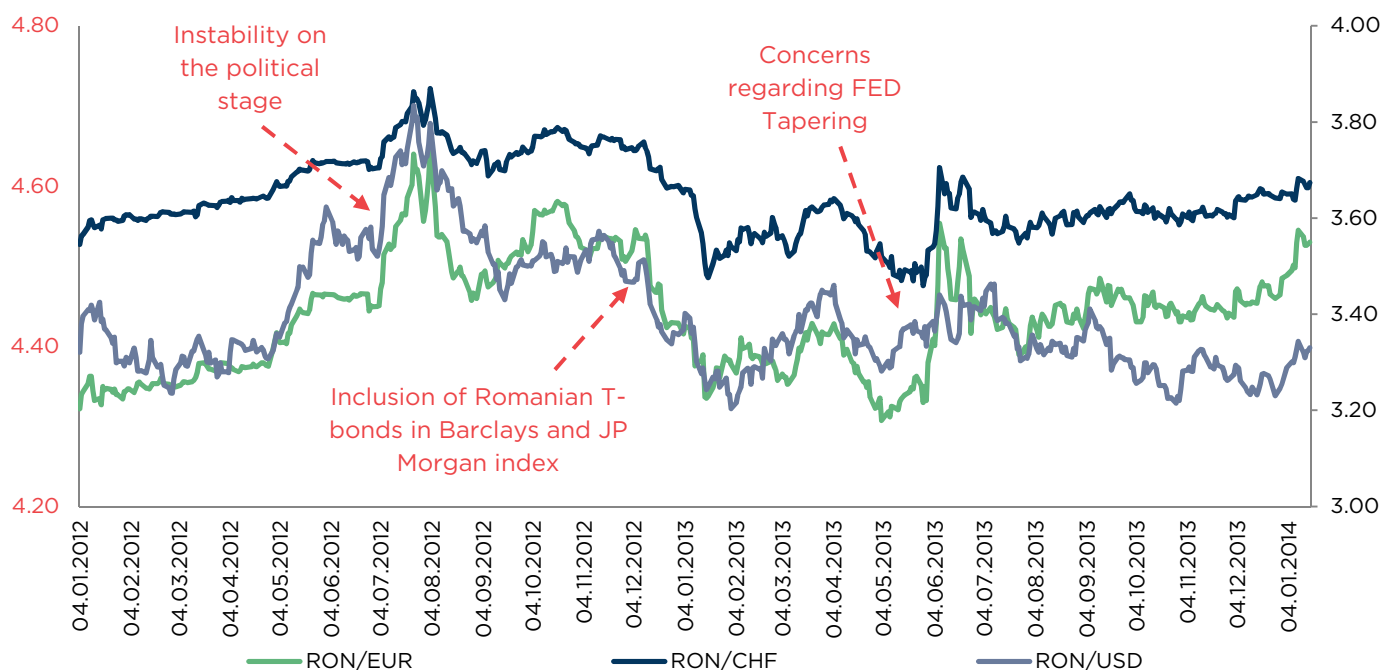
The progress of European funds absorption programs and the issuance of Euro-bonds determined significant capital inflows during 2013, but these were mainly directed towards the treasury of the central bank and did not determine the appreciation of the local currency. The local currency registered one of its best evolutions in the region, from a stability related point of view, recording the lowest volatility¹ during 2013. The stability of the local currency was achieved in the context of setting off the actual capital outflows from the foreign exchange markets (in particular in the context of the dis-intermediation process of the banking sector) against the actual foreign currency inflows (in the context of non-residents' higher demand for T-bonds denominated in local currency).

We estimate that, during 2014, the local currency will continue to show a constant evolution, with more risks concerning a trend of slight depreciations. The main reason is that the growth potential of non-residents' demand for T-bonds denominated in local currency is limited, in the context of extremely low actual yields. Furthermore, the current year will be marked by the reimbursement of an

¹ The standard deviation of the RON/EUR exchange rate time horizon for 2013 was of 0.04, compared to EUR/HUF of 3.34 during the same analyzed period of time.

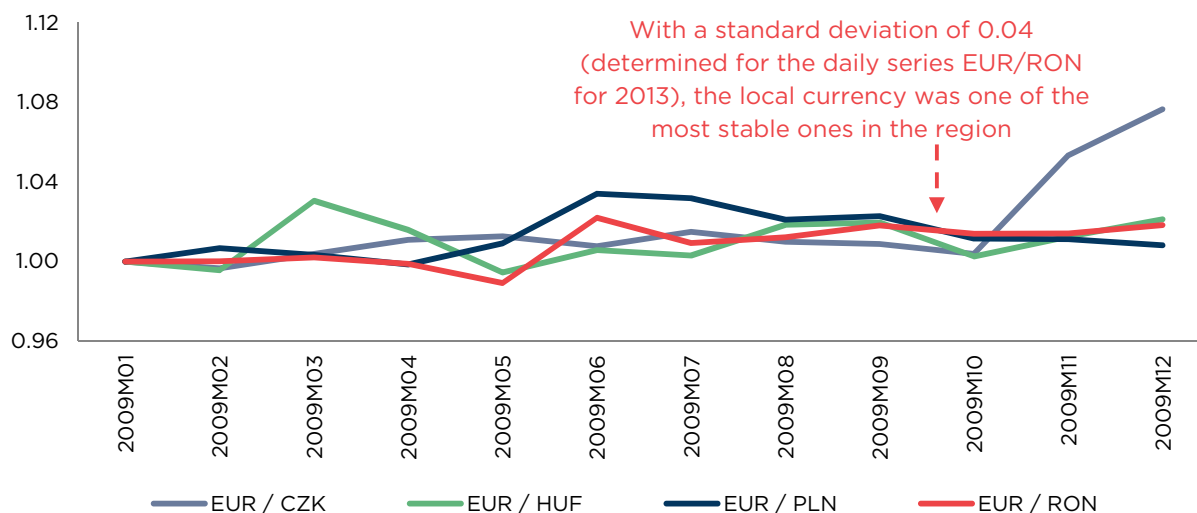
additional installment of 4.7 BEUR to IMF, payment that will be accommodated from the foreign currency reserves of the NBR. The significant side slips of the political stage, as well as the investors' feeling concerning the evolution of emerging markets (with potential portfolio resizing) will have a significant impact on the evolution of local currency compared to EUR. In the basic scenario (that does not consider sudden changes in the FED monetary policy, nor political side slips on the local stage), we estimate an average exchange rate of approximately 4.55 EUR / RON for 2014.

Fig. 19 - Foreign Exchange Rate



Source: NBR, data processed by Coface

Fig. 20 - EEC foreign exchange rate (Jan. 2009 = 100)

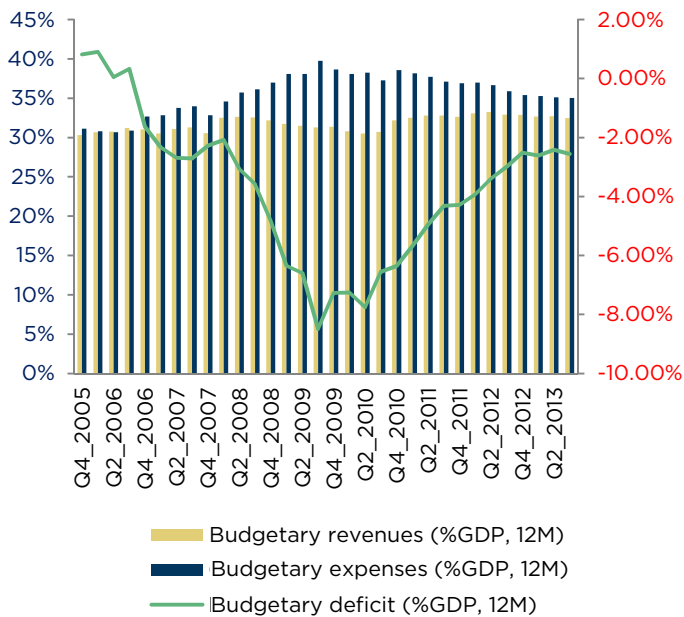


Source: Eurostat, data processed by Coface

5. FISCAL CONSOLIDATION

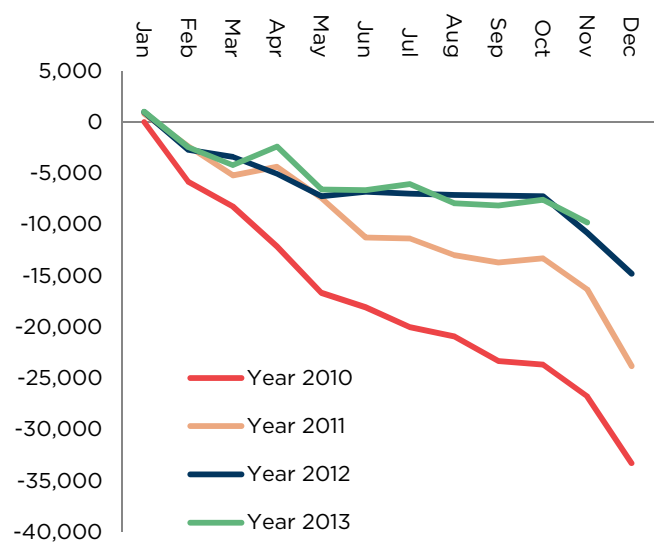
The deficit budgeted for 2013 was revised to 2.5% from (the initial 2.3%) due to the budgetary revenues below expectations, negatively impacted by the poor performance of profit tax collection. The aggregate budgetary deficit for the first 11 months was 9.78 BRON, i.e. 1.6% of the GDP. Thus, the government likely met the revised budget target, even if budgetary expenses increase significantly in the last 2 months of the year.

Fig. 21 - Fiscal Consolidation



Source: MPF, data processed by Coface

Fig. 22 - Budgetary Deficit (MRON)



Source: MPF, data processed by Coface

The budgetary deficit targeted for the next year is 2.2% of the GDP, and the official measures announced by the government regarding the budget are:

- The increase of fuel excises by 0.07 EUR/ L (as of April), with a 5% impact on final prices
- Decrease of CAS by 5pp (conditioned by compensating alternatives that have yet to be clarified)
- Increase of the minimum economy wage to RON 900 in two stages (January and July), as well as the indexing of pensions by 3.76%

The targets are ambitious and unlikely to be achieved in the absence of:

- Alternative measures to compensate for the decrease of fiscal revenues caused by the CAS reduction
- More efficient public revenues collection activity
- A more strict control on budgetary expenses

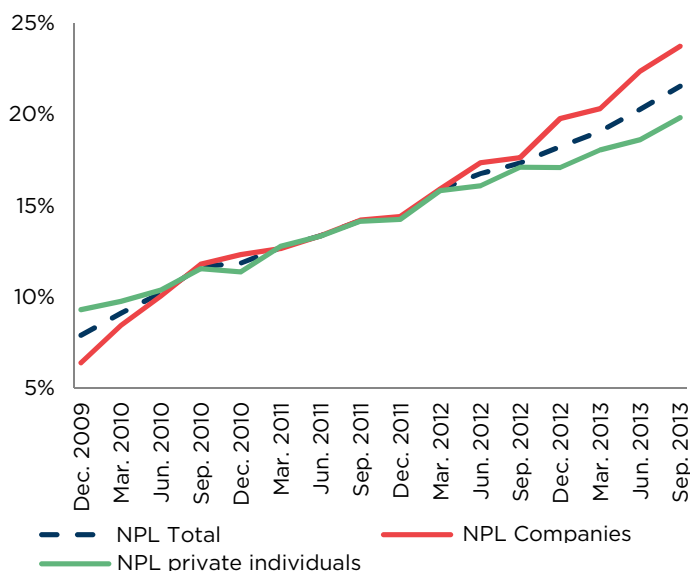
6. FINANCIAL BROKERING

The credit risk may materialize within two channels:

6.1. The banking loan risk - the constrained capacity to honor the debt service related to ongoing loans. During 2014 the banking system remains affected by the high level of bad loans. Furthermore, the banks in the Euro zone, weakened by the crisis of sovereign debt, hold more than 70% of Romanian banking assets. The volume of overdue loans continued to increase during 2013, and, which is more severe, the annual increasing pace did not show significant moderation. Consequently, the weight of bad loans (determined based on the gross exposure, based on the data of prudential reporting) in overall classified loans and interests continued to show an increasing trend, with a 21.6% value of the indicator in September, 2013, compared to the level registered at the end of 2012, of 18.2%.

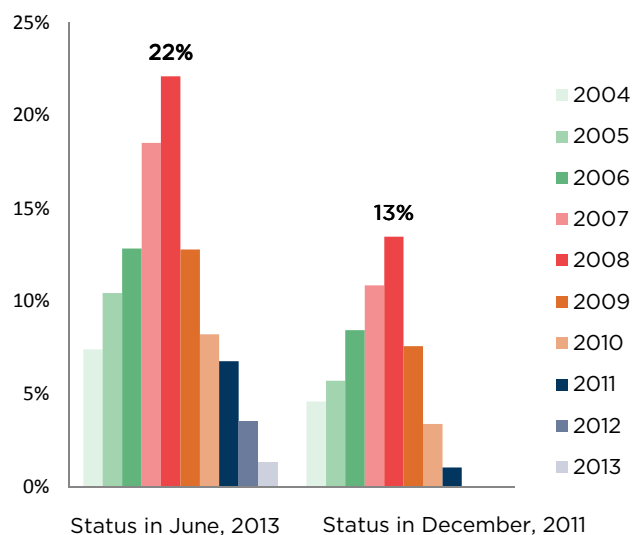
Also, during the last two years we can notice a more accelerated deterioration of the corporate payment discipline, compared to the one registered with respect to the retail sector. Thus, if until 2011 the weight of bad loans of the retail banking sector exceeded the corporate one, as of 2012 things have changed, where the NPL rate among companies reached 23.8%, compared to 19.8% for the retail sector. The loans granted under more lenient terms during the years prior to the crisis continue to affect the quality of banking assets. The loan portfolios with the highest risk are those granted between 2007 and 2008. The non-performance volume generated by these exposures represents approximately 70% of the overall volume of bad loans.

Fig. 23 - Weight of bad loans (NPL)



Source: NBR, data processed by Coface

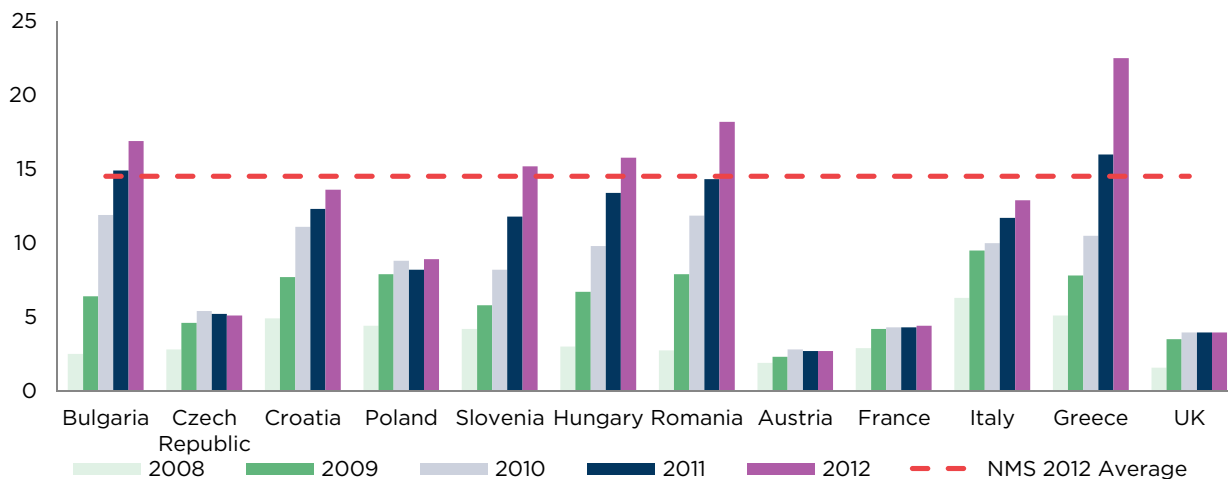
Fig. 24 - NPL depending on the loan granting year



Source: NBR, data processed by Coface

The mentioned evolutions are similar to those registered on other European banking markets (Fig. 25), where the deteriorating process of the quality of loan portfolios mainly affects the countries in the region (for instance Slovenia, Hungary, Bulgaria; the highest level of bad debts was reported by Greece, namely 22.5% with respect to 2012, by 6.5 pp higher compared to the previous year) and, to a lower extent, by the Western European countries. According to the data published by BCE for the end of 2012, at that time Romania registered the highest NPL rate after Greece, with a value of 18.2%, being followed by Bulgaria with 16.9%.

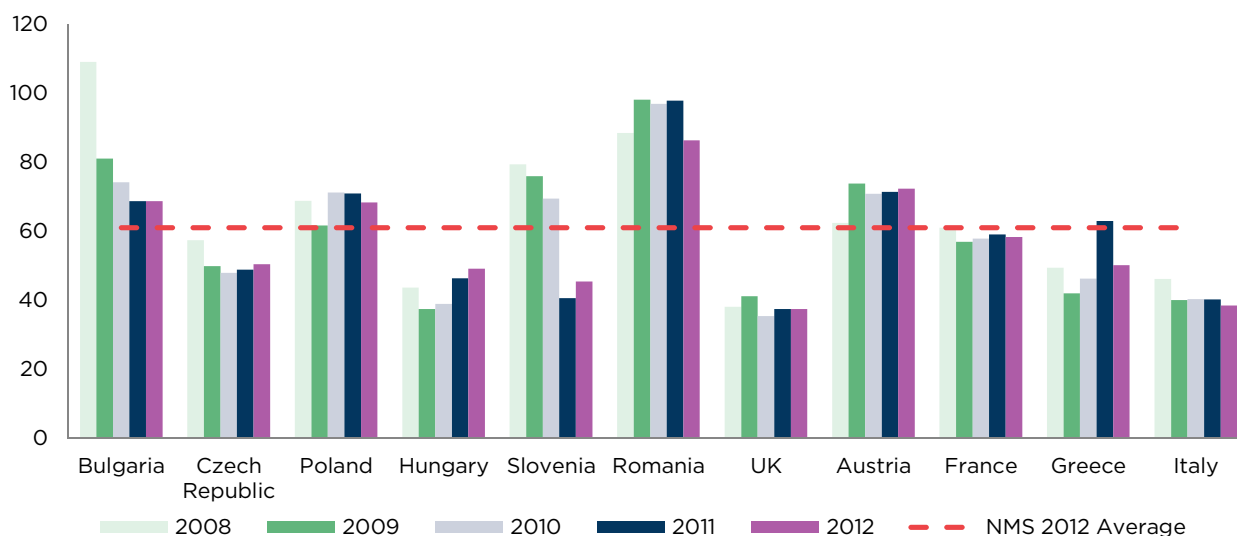
Fig. 25 - NPL, international comparison



Source: BCE, data processed by Coface

The provisioning degree determined at the level of Romanian banking system is the highest one, compared to the one reported by the countries in the region and by the countries of origin of the majority shareholders of credit institutions, Romanian legal entities, which have the status as subsidiaries of foreign banks.

Fig. 26 - Coverage degree of bad loans



Source: BCE, data processed by Coface

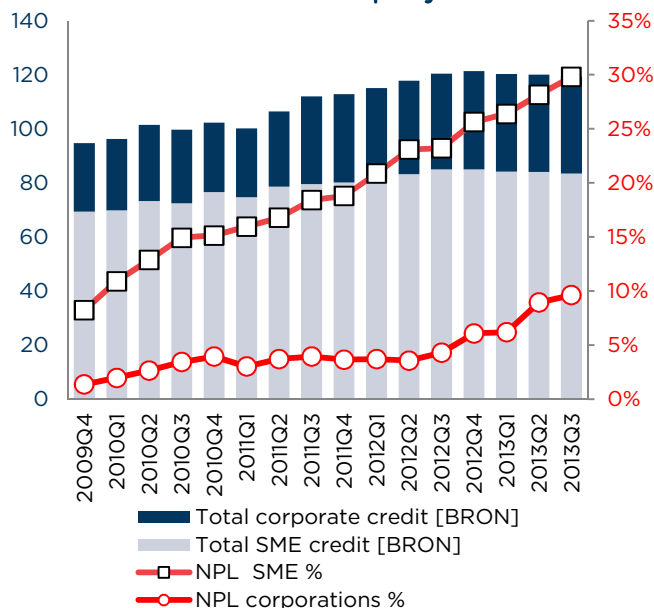
6.2. The commercial credit risk - shows the payment discipline of the corporate environment, and the degradation in this area generates a vulnerability of the financial stability. Most of the aggregate data concerning the evolution of private companies during 2013 confirm a degradation of the payment discipline among companies, and for all segments. Thus:

- **The SMEs** - registered an increase of the weight of bad loans in the context of a more extended term related to the collection of receivables. Between August 2012 and 2013, the debts registered by SMEs to the banking sector increased by 26%, and at the end of August, 2013 the NPL rate among these companies reached approximately 30%.

- **The large and extremely large enterprises** most likely represent the most affected segment among private companies. Between August 2012 and 2013, the arrears registered by these companies to the banking sector increased by 126% (from 1.52 BRON to 3.44 BRON), and the NPL rate increased to 9.62% (August, 2013), by two times compared to the level registered in July, 2012 (4.29%). Some of the reasons that determined this evolution are:
 - **Acceptance of more extended collection terms** - in the context of the financing restrictions that persisted for the last 3-4 years, and which were more acute for the SMEs, the large and very large companies progressively played a more and more significant "commercial bank" role for their customers, by preferring to accept extended collection terms. Thus, during the last years, the SMEs transferred a significant part of the banking credit to the commercial one (supplier credit), this fact intensifying the relations between private companies, which started to show a significant financial side, not only one of commercial nature. Based on these structural economy changes, the effect of contagion and propagation of negative shocks is much faster nowadays.
 - **Decreasing self-financing reserves** - in the context of deteriorated sustainability and self-financing capacity due to the effects of the financial crisis of the last 3 years, as well as of deteriorated payment discipline at the entire economy level. Thus, the large and extremely large companies start to show a higher sensitivity degree to exposure to external or internal shock, with an increased liquidity-related pressure.
 - **Use of the insolvency proceedings** as action for the protection against creditors, the number of insolvencies newly initiated by the debtor party increased during the last 2 years. The permissive insolvency-related legislation most likely had a contribution in the creation of companies' opportunities, in particular of those with majority private capital, to adjust to a low extent based on their own efforts and to a significant extent based on the creditors' account - in particular consolidated budget and banks.

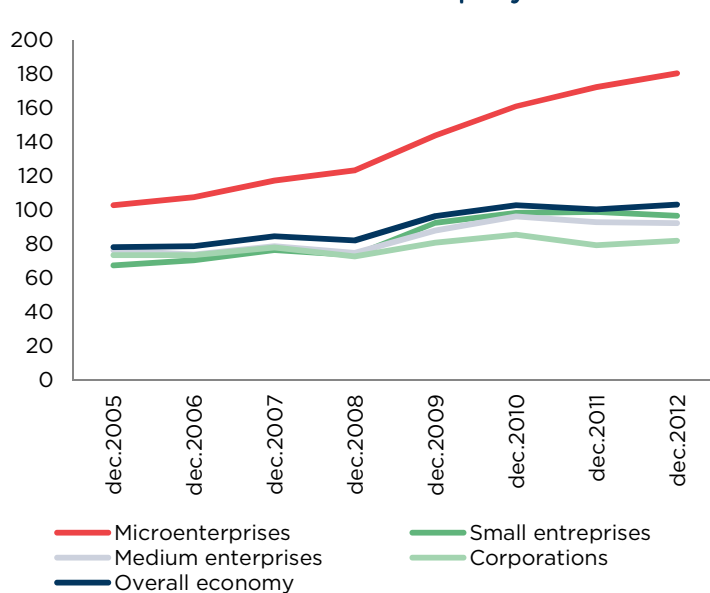
All these reasons and practices caused the initiated insolvency of a record number of medium and large companies. Thus, the number of companies with a turnover higher than 1 MEUR, which became insolvent during 2013, is the maximum number registered during the last 20 years, namely 718 companies, compared to 485 insolvencies of the same category registered during the same period of time of the previous year.

Fig. 27 - Bad loans, depending on the size of the debtor company



Source: NBR, data processed by Coface

Fig. 28 - DSO at economy level, depending on the size of the debtor company



Source: NBR, data processed by Coface

The increased number of medium, large and very large companies which became insolvent determined the increase of the average value of payment incidents reported to CIP, based on an increased value of incidents and a decreased number of chargebacks (the large and very large companies may register a lower number of transactions, but with a much higher average value than the rest of the companies).

Also, according to the data published by CIP², the amounts refused for payment with debit instruments during the first 11 months of 2013 had a total worth of 8.6 BRON, by 8% higher compared to the same period of time of the previous year. While the number of payment incidents during the same analyzed term decreased by 14%, the average value of payment incidents increased by 26%. Thus, the average payment incidents registered between January and November, 2013 amounted to 59 KRON, compared to the level registered during the same period of time of the previous year, namely 47 KRON.

Furthermore, we can notice that the value of payment incidents registered during the first 11 months of 2013 are by 2% higher compared to the similar period of time of 2009, where the average value of chargebacks is by 2.1 times higher. Irrespective of the underlying reasons (more balanced scenarios may exist, and show that the payment instruments were more rarely used in practice), the evolution is extremely worrying, because 2009 marked the more severe contraction of the local economy of the last 10 years and the first year when the effects of the world crisis were felt at local level.

² Payments Incidents Register, NBR

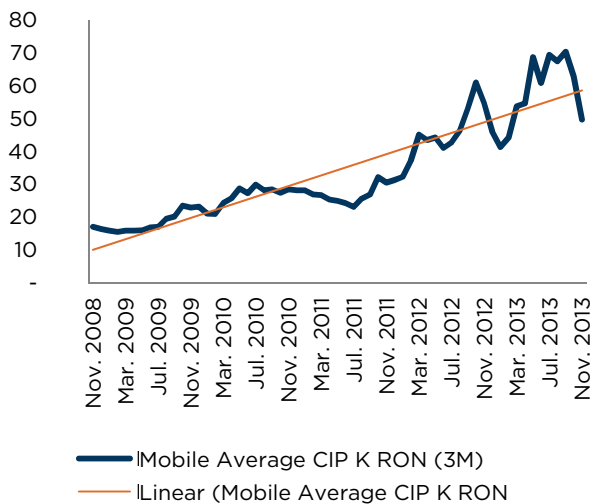
Evolution of payment incidents reported by NBR

Total January - November	Total amounts refused for payment	Number of incidents	Average value per incident	Amounts CIP %	Number CIP %	Average CIP%
Year 2013	8,654,763	145,657	59.42	8%	-14%	26%
Year 2012	8,000,695	169,590	47.18	38%	-6%	47%
Year 2011	5,779,567	180,283	32.06	19%	-44%	115%
Year 2010	4,843,915	324,815	14.91	-43%	-28%	-21%
Year 2009	8,526,167	451,008	18.90	129%	84%	24%
Year 2008	3,724,866	244,632.0	15.23			

Source: NBR (CIP), Data processed by Coface, The figures are expressed in KRON

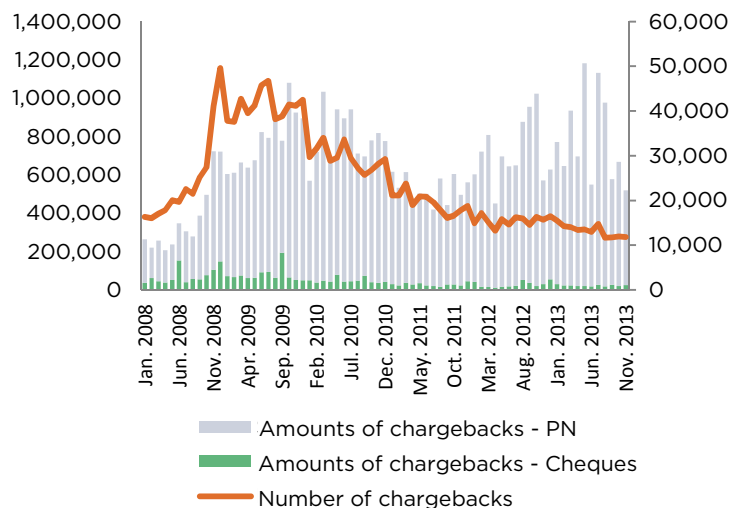
In line with the extension of the receivables collection term from economy, the tendency may indicate a deterioration of the payment behavior regarding the observance of debit instruments, which might cause the companies to require the partial or full payment in advance in order to protect themselves against the commercial credit risk.

Fig. 29 - CIP average value (KRON)



Source: BPI, Data processed by Coface

Fig. 30 - Number of payment incidents and charged back amounts (KRON)



Source: NBR, data processed by Coface

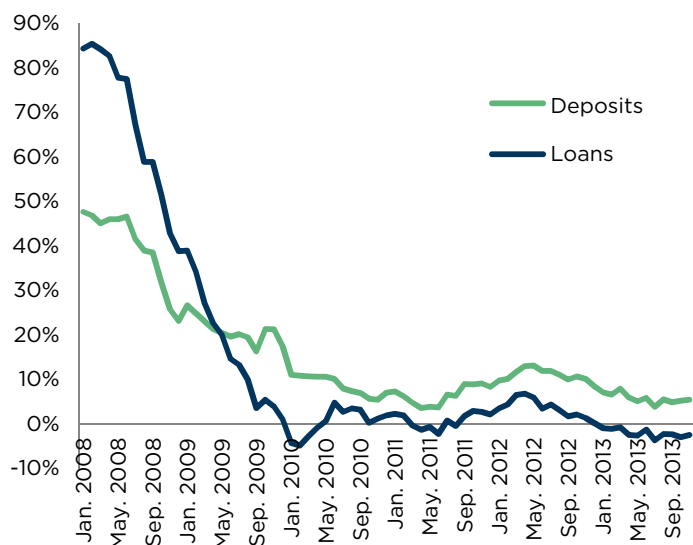
Evolution of Loan Balance vs. Deposits in the banking sector

Indicator	Nov 2013 / Nov 2012	H1 2013 / H1 2012	Q1 2013 / Q1 2012
Non-performing Loans (RON)	↑ 23.81%	↑ 24.41%	↑ 24.43%
Non-performing Loans (Foreign Currency)	↑ 15.91%	↑ 32.94%	↑ 38.71%
TOTAL Non performing Loans	↑ 18.94%	↑ 31.23%	↑ 32.68%
Individual Loans Balance	↓ -2.49%	↓ -1.24%	↓ -0.74%
Non-financial Companies Loans Balance	↓ -5.40%	↓ -1.33%	↑ 0.26%
Individual Deposits Balance	↑ 5.38%	↑ 5.83%	↑ 7.90%
Non-financial Companies Deposit Balance	↑ 9.81%	↑ 5.81%	↑ 2.31%

The analysis of the evolution of loans granted to the private sector, based on the debtor categories, shows the following trends:

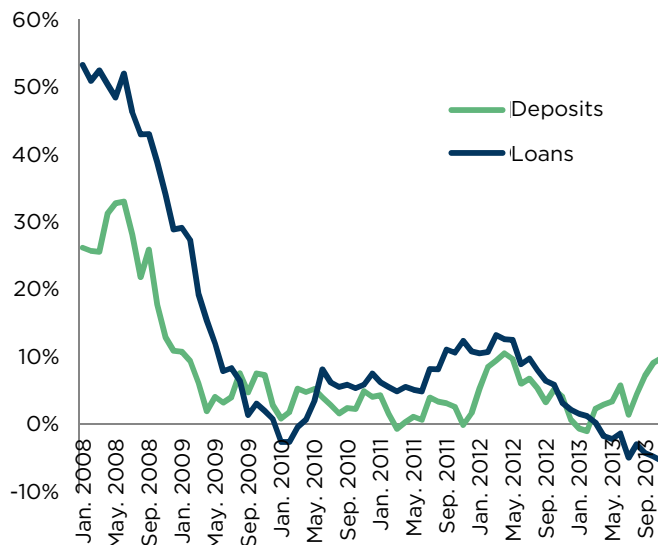
- The balance of loans granted to the public households at the end of November, 2013, amounted to 103 BRON, by 2.5% lower than during the same month of the previous year. The number of CRC interrogations (Central Credit Register) performed by the credit institutions with respect to potential debtors between January - November, 2013 amounted to 991,044, level almost identical with the one registered during the same period of time of the previous year. Under these circumstances, the loan demand most likely stagnated during 2013.
- The deposits set up by public households at the end of November, 2012, amounted to 129 BRON, by 5.3% higher, compared to the same period of time of the previous year, and the increase registered during 2013 was constant throughout the year
- The process of financial dis-intermediation is more accelerated in case of companies, where the balance of loans granted to non-financial companies decreased by -5.4% in November, 2013 **compared to the balance registered during the same month of the previous year.**
- The level of deposits set up by non-financial companies in the banking system registered a significant increase during the first 11 months of 2013, with a registered increase by approximately 10%

Fig. 31 - Loans V.S. Deposits of the public households (year-over-year)



Source: NBR, data processed by Coface

Fig. 32 - Corporate Loans V.S. Deposits (year-over-year)



Source: NBR, data processed by Coface

Total Interrogations with the Central Credit Register

Year	Total interrogations concerning own debtors (proxy for current portfolio risk management)	Total interrogations concerning potential debtors (proxy for the demand of new loans on the market)
2008	80,853	9,391,691
2009	903,476	1,832,117
2010	927,129	1,504,744
2011	927,129	1,504,744
2012	847,311	1,068,978
2013 (Jan-Nov)	828,410	991,044

Source: NBR, data processed by Coface

Thus, we can appreciate that the "deleveraging" process can be found both among the general public and among the private non-financial companies, with a higher frequency among the latter. A higher precaution regarding the credit and consumption appetite is also confirmed by the stagnating demand for new loans (through the volume of CRB interrogations concerning potential debtors) and which has a level of approximately 10 times lower than the one registered in 2008. The incapacity of the banking sector to invest the liquidity surplus under extremely advantageous credit terms, in particular for loans denominated in local currency, confirms the reluctance of economic operators concerning the crediting process, in the context of incertitude and a low level of consumer confidence, at the minimum threshold of the EU zone (28).

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