

Romania monthly economic review

October 2008

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Cabinet approves draft central budget for 2009

The government approved the draft central budget for next year based on GDP growth projections of 6% and a deficit target of 2.2% of GDP. The general budget deficit is projected at 2% of GDP next year. We recall that the central government budget includes the vast majority of tax revenues but part of them are redistributed to local governments that run separate budgets. In addition, the social security budget and the budgets of other state entities (e.g. public motorway company) are added as part of the general government budget. The Prime Minister, Calin Popescu-Tariceanu, stressed that the budget is designed to address the future economic challenges as it stipulates larger share of investment spending at the expense of current spending. The payroll in the budgetary sector is estimated to shrink to 5.9% of GDP from 6.3% this year while the capital spending would reach 6% of GDP from 5.6% this year.

Budget deficit of 1.08% of GDP, after 8 months

General consolidated budget ended the first 8 months of this year in a deficit of 1.08 of the GDP, the negative balance being RON 5.137 bn, according to data made public by the Ministry of Economy and Finance (MEF). After the first 7 months, the consolidated deficit stood at 0.64% of the GDP. Budget revenues stood at RON 107.43 bn or 22.6% of the GDP over January-August while expenses at RON 112.56 bn or 23.7% of the GDP. The most important cashing resulted from insurance contributions - RON 31.342 bn (6.6% of the GDP), VAT – RON 27.82 bn (4.8% of the GDP). The most important expenses were allotted for social assistance -RON 33.62 bn (7.1% of the GDP), staff – RON 22.35 bn (4.75 of the GDP) and goods and services – RON 20 bn (4.2% of the GDP). The budget deficit target for 2008 was set at 2.7% of the GDP, through the draft budget, with the deficit level being afterwards cut to 2.3% of the GDP through budget rectification. The International Monetary Fund (IMF) recommended Romania a budget deficit of 1.75% of the GDP for this year. The GDP in 2008 is estimated at RON 440 bn.

Ernst & Young SRL

Premium Plaza Building, 3rd Floor
63-69, Dr. Iacob Felix Street
Sector 1, 011033 Bucharest
Tel: (40-21) 402 4000
Fax: (40-21) 310 7193
Email: office@ro.ey.com
www.ey.com

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Deficit in balance of payments worth more than EUR 10 bn

Current account of balance of payments for Romania recorded a deficit worth EUR 10.006 bn January through August this year, that represents a 1.6% growth when compared to the same interval in 2007, the Romanian National Bank (BNR) announced. The decisive influence of the current account balance was given by the deficit in the trade balance, which stood at EUR 11.714 bn, which is an increase by 8.1% as against the January-August interval in 2007. The dynamics of exports outrun by 3.7% the dynamics of exports in the first 8 months of the year. The current account deficit in the January-August interval was covered 65% with FDI, which registered EUR 6.50 bn, out of which participations to the capital and reinvested profit represented 53.3%, with the intra-group credits standing at 46.7%. The foreign debt on a medium and long term recorded on 31 August 2008, the level of EUR 47.461 bn, which is a 23.3% growth as against the level on 31 December 2007. The foreign public debt and publicly guaranteed, hit a balance standing at EUR 10.635 bn on 31 August 2008 and represented 22.4% of the foreign debt on a medium and long term (as against 26.5% on 31 December 2007). The publicly non-guaranteed foreign debt stood at EUR 30.646 bn on 31 August 2008, that is an increase by 22.3% against that on December 31, 2007. The foreign debt service rate on a medium and long term stood at 24.3% over January-August, compared with 21.8% in 2007. The coverage rate stood at 5.6 months of imports of goods and services on 31 August 2008, as against 6 months on 31 December 2007.

Industrial production up 4.9% in 8 months

The industrial production increased with 2.9% during the first 8 months of the year, compared to the similar period of the previous one, and the respective increase was achieved due to the processing industries (that reached an increase of 5.3%), electricity and thermal energy, water and gas production (+7.2%) according to preliminary data announced by the National Institute of Statistics (INS). During the mentioned period, the extractive industry decreased by 0.7%. Analyzing the major industrial categories, there are registered increases in the tangible assets industry (+10.6%), everyday goods and services (+8.4%), intermediary goods (+2.1%) and the electricity industry (+1.5%). On the other hand, the supplies of primary energy sources and the electricity sources increased by 0.5% and respectively 0.8% throughout January-August, compared to the previous 8 months of the last year. The top primary energy sources totaled 27.41 mn tonnes of oil equivalent. The total turnover for retail, except for car and motorcycle sales, increased with 16.6% during the first 8 months of this year, compared to the similar period of the previous one, according to INS. The increase achieved during the initial 8 months of the year is caused both by non-food products sales that increased with 18.9% as well as food products, beverages and tobacco products sales that increased by 14%.

Annual inflation decreased to 7.3% in September

The annual inflation (September 2007 – September 2008) decreased in September 2008 to 7.3% as against 8.02% in August, based on the data released by the National Institute of Statistics (INS). Compared with the previous year, consumer prices advanced by 0.4% in September. Compared with September 2007, the food products prices cost went up with 7.08%, service fees advanced by 7.75%, and non – food products were by 6.6% more expensive. Compared to August 2008, in September 2008, the prices of food products advanced by 0.33%, those of non – food, by 0.19%, whereas the service fees advanced by 1.05%. According to analysts, the advance of consumer prices in September, which exceeds the expectations, was entailed by the depreciation of the national currency. "There is a strong growth in case of services because of the exchange rate depreciation. We need to maintain the exchange rate below RON 4/ EUR. Based on the data

published on Friday by INS, the trade deficit has advanced in the first 8 months of the year, compared to the corresponding amount of time in 2007, by 9.35%, and it amounted to EUR 14.58 bn. During this time, imports continued to outperform exports. Thus, exports advanced, over January–August, by 18.3%, to EUR 22.63 bn, and imports advanced by 14.6%, to EUR 37.2 bn. FOB exports, made during the first 8 months of 2008, amounted to RON 82.447 bn (EUR 22.636 bn) and CIF imports amounted to RON 135.570 bn (EUR 37.215 bn).

Economic indicators in industry to deteriorate

A deterioration of the perspective of the economic indicators in industry and constructions is possible in the coming months, the experts of the Romanian National Bank (BNR) estimate in a survey. Although in October the evolution was still positive, “on a much longer horizon, there are signs of worsening,” the survey shows. Thus, according to BNR analysis, the volume of production has maintained the upward trend in the 2 economic sectors which were analyzed, the rate acceleration showing a circumstantial balance of +33%. This estimate could prove however too optimistic, in the conditions in which recent declarations show the beginning already in October of a period of adjustments of production in important industrial sectors, on the background of the tempered demand both internally and internationally. In the constructions sector, the seasonal decrease of the growth rate of the portfolio of orders is expected. The main factors which can act as a brake on the good evolution of the production process in industry and constructions remain the insufficient demand (mentioned by 25% of the respondents), the evolution of the exchange rate and the difficulties to cash the equivalent of the sold production. Moderate inflationary pressures are anticipated in constructions, most of the answers pointing to price stability.

S&P concentrated unfairly on Romania lowering the country’s ratings

Standard&Poors (S&P) concentrated unfairly on Romania through the decision to lower the rating, under the conditions where the deficit of current account started to lower as share in the GDP similarly to the speed of credit growth, the Counselor of the National Bank of Romania (BNR) Governor Lucian Croitorul said. The current account deficit started to lower (as share in the GDP). I think that, in the case of S&P, it was about the tendency to negative arguments. It is true that the international climate has worsened, but I think they concentrated unfairly on Romania, Croitoru explained. The BNR Governor Counselor underlined the fact that the deficit of current account was at a high level last year as well and during the last months, the authorities took measures to lower the economic imbalance by referring to the BNR. Over the first 8 months of this year, the current account deficit of Romania grew insignificantly, by 1.55% up to EUR 10.006 bn, from EUR 9.853 bn over the same interval of 2007, according to the data published by the BNR. Over the first semester of the year, Romania’s economy grew by 8.8% the GDP reaching EUR 53.3 bn. The S&P analyst, Marko Mrsnik argued, in the announcement of the rating agency, that the decision-makers attacked the most important economic issues, in the context where the attention changed towards general elections to come, which increased trouble and lack of cooperation in the political environment. Croitoru mentioned as main consequence of Romania lowered rating, the increase in foreign financing, but he does not consider that this will reflect in a slowing down of economic growth of Romania for 2009. The decision could affect negatively the volume of foreign direct investment in Romania, the BNR official concluded.

Moody's sees no reasons for imminent rating action

International rating agency Moody's maintains a stable outlook on the country's investment-grade sovereign rating (Baa3/stable), estimating the current level as "very well positioned," according to the agency's senior economist Kenneth Orchard. The coming years will be challenging for the country's economy, but the agency foresees no severe crisis and the long term prospects remain very good. The fiscal policy is a concern and the new government will have to tackle the shrinking budget revenues, he added though. Separately, the rating agency Fitch estimates that Romania's economic growth would decelerate under the circumstances of shrinking lending and it anticipates rising general macroeconomic risks but mentions no imminent rating action. Fitch maintains a one-notch differential above Moody's and two-notch differential above S&P (BB+/negative) on the country's sovereign rating (BBB/negative). The main macroeconomic risks are generated by the external financing and by the impact of the exchange rate volatility on the banking system due to the large share of foreign currency in the stock of loans. A hard landing episode might be triggered by scarce external financing in case the foreign investors lose confidence in the country's fundamentals or in case their risk aversion further increases.

Romania's economic growth projected at 9.1%

Romania will achieve an economic growth of 9.1% this year and 6% in 2009, according to the National Prognosis Commission (CNP). According to their latest report, services will lead the growth with an input of 3.4%, while agriculture will grow 15.2% after last year's regress and generate 1% of growth. The nominal GDP will reach RON 505 bn and slow down the growth rate to 6.3% in 2010 and 6% in 2012 and 2013. At the end of this year, the trade deficit will reach EUR 23.85 bn, equal to 17.3% of the GDP. The forecast for the near future indicates that the trade deficit will deepen, but its weight in the GDP will gradually decrease to 10% in 2013. Exports will reach EUR 34.85 bn at the end of this year, up by 18% year-on-year, while imports have been projected at EUR 58.7 bn, up by 14.4% year-on-year. The current account deficit will reach EUR 18.13 bn, down by EUR 540 mn from the previous forecast. The foreign deficit will reach 7.5% of the GDP at the end of 2013, down from an estimated 13.2% this year. Eight months through this year, the current account deficit stands at EUR 10.006 bn, compared to EUR 9.853 bn in the corresponding period of 2007. The inflation rate for this year has been estimated at 6%, up from the previous estimate of 5.8%. However, the National Bank has released a different forecast, of 6.6%, up by 0.6% from their previous estimate. The forecast for the next few years points to 4.5% in 2009 and a historical low of 2.32% in 2013.

Employment and wages

Romania's August net salary down 2.4%

Romania's net average salary was down 2.4% on the month in August to RON 1,277, according to the National Institute for Statistics. In nominal terms, the salary was RON 31 lower compared with RON 1,246 in July. In real terms, wages were 2.8% lower on the month, but 122% higher than in October 1990. Air transport employees saw the biggest average net salaries of RON 3,188, while employees in the clothing industry were at the opposite pole with RON 731. August net average salary in agriculture was up 0.3% on the month to RON 897. Net salaries in the industrial field averaged RON 1,200 in August, down 3% from July salaries. In the energy field, average net salaries in August were RON 1,958, 5.9% lower than in

July. On the year in August, average net salary in Romania rose 14.8% in real terms.

Workforce shortage will offset layoffs from other sectors

Although signs of the financial crisis are being felt on the local market, there is no reason to panic yet, said Labour Minister, Marian Campeanu. "Growth percentages have been repositioned. Yet it is growth, which means we will not see many layoffs. Moreover, we have a labour shortage that can offset the layoffs from other sectors. There is no reason to panic," Campeanu said, adding that, although the crisis is just beginning, part of the negative effects of the financial crisis has been overcome. Romania has been through a long transition and, on an institutional level, is prepared to deal with higher unemployment than before. Unemployment could be higher than this year, when it reached 3.9%, though not significantly higher, at least not in the first half of next year. The Minister believes that a debate should be started in terms of a greater flexibility of the conditions on the labour market, so as to allow companies to hire people for shorter periods of time, when they are on the rise and then make their employees redundant in case the business is slower. Due to the fact that the current conditions in the labour legislation are very restrictive, the future government should start a debate on how the Labour Code could be modified. As for the debate on the teachers' salaries, Campeanu says that no country in the world can grant 50% pay rises when the economy only grew by 9%, labour productivity by 13-14% and inflation stood within reasonable limits.

Developments in tax legislation

MEF published the amended draft of the Fiscal Code

The Ministry of Economy and Finances (MEF) published the draft amending the Fiscal Code, which provides for exemptions from the tax on the profit made on stock exchange transactions in 2009 along with other deductions. According to Minister Vosganian the deductions will lower the revenues by RON 538 mn. Based on the Ministry calculations, the total invoice to the budget triggered by the fiscal gift will indicate RON 538 mn; out of them, RON 470 mn result from tax exemptions on gains made by individuals from transfer of securities, in case of close companies. Other RON 37 mn result from profit tax exemption in case of foreign companies, and RON 31 mn are the result of exemption on the tax on the profit made by Romanian companies. The negative impact on the budget, estimated by the Ministry, is equivalent to EUR 151 mn, at the average exchange rate estimated by National Commission for Prognosis for next year, which is RON 3.55 / EUR. This accounts for 0.09% of GDP, which is estimated at RON 529.9 bn in 2009. Regarding the income tax, for the fiscal year 2009, the tax calculated using 1% tax quotas and 16%, respectively, on the gains made by individuals in the capital market, will be suspended. In addition to this measure, the law will secure also the forward carrying over of the loss registered by that individual in the next fiscal year from the net gains having a similar nature, established in a differentiate manner by the 2 types of securities owned during the ownership interval, below 365 days and over 365 days respectively. On the other side, the amounts absorbed by ISPA funding programme will exceed, in 2008, EUR 350 mn, and they are expected to be around EUR 500 mn in 2009, according to Eugen Teodorovici, MEF State Secretary.

Foreign direct investments in Romania

FDI up 60% to EUR 6.5 bn in first 8 months

Foreign direct investments (FDI) have grown by 60% in the first 8 months of this year compared to the same period in 2007, reaching a level of EUR 6.502 bn, a level that has covered 65% of the foreign deficit, the data published yesterday by the Central Bank shows. After the first 8 months of 2007 the FDI totaled EUR 4.06 bn, a value that covered only 40% of the current account deficit registered at that time. Of the total FDI registered in Romania in the January-August time period, the capital participations and the reinvested profits have represented 53.3%, while the intra-group credits represented the remaining 46.7%. However their share in the FDI has dropped in the first 8 months of 2008 compared to the same period last year, back when the intra-group credits represented 51.3% of FDI. In August the FDI registered a level of EUR 733 mn, after totalling EUR 5.769 bn in the first 7 months. Last year the FDI dropped by 22.3% to EUR 7.069 bn and covered 41.9% of the balance of payments deficit. Romania's current account deficit has almost stagnated after the first 8 months of the year, after it previously grew by 12% in July, on the backdrop of higher inflows from current transfer payments and the hiking of the balance of services surplus in August, factors that have compensated the hike of the trade deficit, the BNR data shows. Thus, the balance of payments deficit in the first 8 months of this year stood at EUR 10.006 bn, compared to EUR 9.853 bn in the same period last year. After the first 7 months of this year, Romania's current account deficit grew by 11.9% compared to the level registered in the same period in 2007, reaching a level of EUR 9.4 bn. Over the January-August period, the trade deficit – the main source that fuels the external imbalance – has tempered its growth rhythm to 8.1% compared to last year, reaching a level of EUR 11.7 bn. The balance of services has registered a surplus of EUR 688 mn in the first 8 months, up by 61.9% compared to the level registered in the same period in 2007. In the first 7 months the balance of services surplus was up by 70.5%. The income account deficit has grown significantly – by 18% – from EUR 2.86 bn in January-August 2007 to EUR 3.38 bn in the first 8 months of this year. The transfer payments, mostly including the remittances from Romanian workers abroad, have totalled EUR 6.124 bn in the first 8 months, up by 29% compared to the level registered in the same period last year. According to BNR, at the end of August Romania registered a medium and long-term foreign debt of EUR 47.46 bn, 23.3% higher than the one registered at the end of 2007, as a consequence of the growth of the direct public debt and of the publicly non-guaranteed debt.

Bucharest, Europe's third choice for business expansion

Bucharest is the third city in Europe where the continent's top 500 multinationals are planning to expand their business according to the 19th edition of the European City Monitor (ECM), a report issued annually by the real estate consultants Cushman & Wakefield. Bucharest is outranked by Moscow and Prague, tied with Warsaw and outranks Budapest. Polled by Cushman & Wakefield, the top 500 companies in Europe believe that Bucharest is making an effort to improve the business climate, but not as big an effort as Barcelona or Madrid, which lead the race for pleasing corporations looking to set up shop in a new city. When it comes to transportation, the perception is that Bucharest has improved internal transportation and therefore moved up from 30th to 26th as far as this subject is concerned. Budapest ranked 31st, Warsaw 30th and Prague also 26th. External transportation is a totally different subject, as Bucharest placed last among the top 34 European cities of importance business-wise, while Budapest moved up from 33rd to 26th. In terms of access to markets, Bucharest moved up 8 spots to 24th and tied with Stockholm and Istanbul. Rome, Vienna and Athens ranked below.

Budapest (22nd), Prague (21st) and Warsaw (15th) did better. London placed 1st. Bucharest managed to secure the 2nd position based on the cost of labor, but multinationals are hardly pleased with the qualification of Bucharest employees and placed the city on the 32nd position. Besides a low cost of labor and plenty of room for quality of labor improvement, Bucharest is also offering tremendous opportunities to improve the quality of life for the employees, as the city managed to place 31st in this department. The top five criteria that do matter are qualified labor availability, easy access to markets, customers and consumers, telecom quality, transportation networks and the cost of labor. Bucharest has managed to improve its perception in terms of pollution and moved up from 32nd to 30th. Getting office space in Bucharest is no longer as cheap as it used to be. The city fell from the 2nd position last year to the 13th. Office space in Bucharest is both expensive and hard to get, as the availability indicator plunged a whopping 18 spots to the 28th position. Telecommunications have improved in Bucharest and the city now stands in the 29th position (32nd last year), above Budapest, Warsaw and Prague, which share the 31st position. The authorities' financial efforts to encourage business (such as tax cuts and other incentives) placed Bucharest on the 11th position, down by one from last year. Despite being the 3rd choice for business expansion in Europe, only 14% of the respondents believe that Bucharest is a known venue for business. London is by far the most popular (82%), while Paris is second (77%). Moscow should be expecting the highest number of multinationals in the next 5 years.

EU integration challenges for Romania

713 applications for European ROP funds

A number of 713 projects in the value of EUR 2.154 bn submitted for financing before 10 October 2008 within the Regional Operational Program (ROP) 2007-2013, are in various stages of evaluation and contracting, stated Sava Marin Chiser, Senior Adviser in the Department for Strategy and Programs Coordination with the Ministry of Development, Public Works and Housing (MDLPL), on the occasion of the Conference on Structural Funds in Romania. "We asked interested parties to come up with projects in all intervention fields of ROP priority axes, with the exception of the first priority intervention axis - Supporting the sustainable urban development - going to be launched in November 2008", according to MDLPL official. "A number of 132 transport infrastructure projects were submitted, in a total value of approx. EUR 1.57 bn. The asked amount is of approx. EUR 1.28 bn, 37% higher than the funds allocated to this priority axis on the entire program period, of EUR 876.7 mn". In the transport field, a number of 17 projects have been contracted or are in a finalization stage, whose overall value exceeds EUR 257 mn, according to the quoted source. The amount from non-reimbursable funds for the 17 projects is of more than EUR 200 mn, accounting for 23% of the total earmarked for this ROP axis.

Key macroeconomic indicators

Years	Months	Employed people (y/y change) ¹⁺²	Monthly net average wage (RON) ²	Registered unemployment rate (% of labour force) ²	Consumer Price Index (% y/y, end of period) ¹	Central + Local Budgets (% of GDP)	Exports (EUR million, fob) ¹	Imports (EUR million, cif) ¹	Trade balance (EUR million, fob-cif) ¹	Monthly FDI, net (EUR million) ²
(0)	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
2007 out of which:										
	August	2.8%	1030	3.90	4.96	-0.19	2240	4046	-1806	4139
	September	2.9%	1040	3.90	6.03	-0.30	2486	4176	-1690	5138
	October	3.0%	1084	4.10	6.84	-0.37	2819	5023	-2203	5958
	November	2.8%	1121	4.20	6.67	-1.44	2763	4986	-2223	6644
	December	3.1%	1266	4.10	6.57	-3.09	2253	4325	-2072	7069
2008 out of which:										
	January	2.5%	1200	4.30	7.26	+0.20	2487	3900	-1413	663
	February	2.2%	1134	4.30	7.97	-0.20	2826	4338	-1512	475
	March	2.1%	1192	4.20	8.63	-0.40	2706	4698	-1992	450
	April	2.2%	1282	3.90	8.62	-0.20	2723	4827	-2104	1630
	May	2.0%	1248	3.80	8.46	-0.80	2971	4754	-1783	768
	June	1.8%	1273	3.80	8.61	-1.50	3034	5047	-2013	772
	July	1.8%	1308	3.80	9.04	-1.10	3190	5077	-1887	924
	August	-	1277	3.87	8.02	-	2619	4330	-1711	754
	September	-	-	3.90	7.30	-	-	-	-	-

Sources: ¹ INSSE ² National Bank of Romania (Monthly Bulletins) ³ cumulated from the beginning of the year, compared with the same period of previous year

Notes: - No data available