

# Agenda

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- 1 Consumer spending
- 2 Industrial Production
- 3 Structural issues for companies
- 4 Demographic challenges



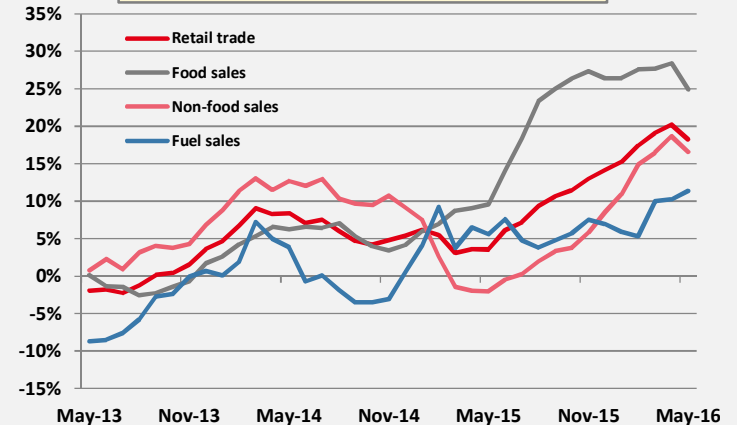
# Consumer spending is the main driver of GDP growth

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## Key Takeaways

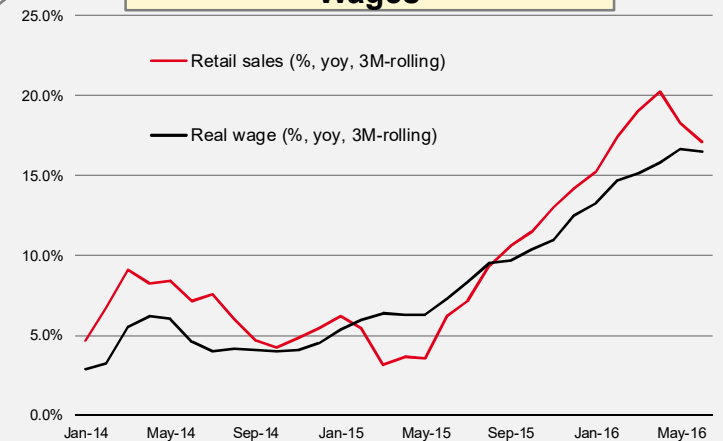
- **Economic growth accelerated above 4% in 2016**, but GDP structure is not balanced and a slowdown is imminent for 2017
- **Consumer spending** is the main driver of GDP growth, following a double digit increase in retail sales:
  - Rapid increase in the average wages due to: **sequential hikes in the minimum wage** and **higher salaries in the public sector** in the run-up to Parliamentary elections
  - Two consecutive reductions in the VAT rate: **VAT for food products was cut to 9%** in June 2015, while the **general VAT rate was lowered to 20%** in January 2016
  - Inflation hovered around very low levels due to the **low global food and oil prices**, thus helping stimulate households' purchasing power
  - **Historically low interest rates** (3M Robor declined to 0.75% in 2016 from 1.33% in 2015) have lowered the debt service for consumers, effectively unlocking additional disposable income
  - **Consumer confidence** returned to levels last observed in the boom period of 2005-2008
- European Commission forecasts indicate **2016 will be a strong year for agriculture**, as the harvest output was boosted by technical crops such as rapeseed

## Retail Sales



Data source: NIS

## Wages



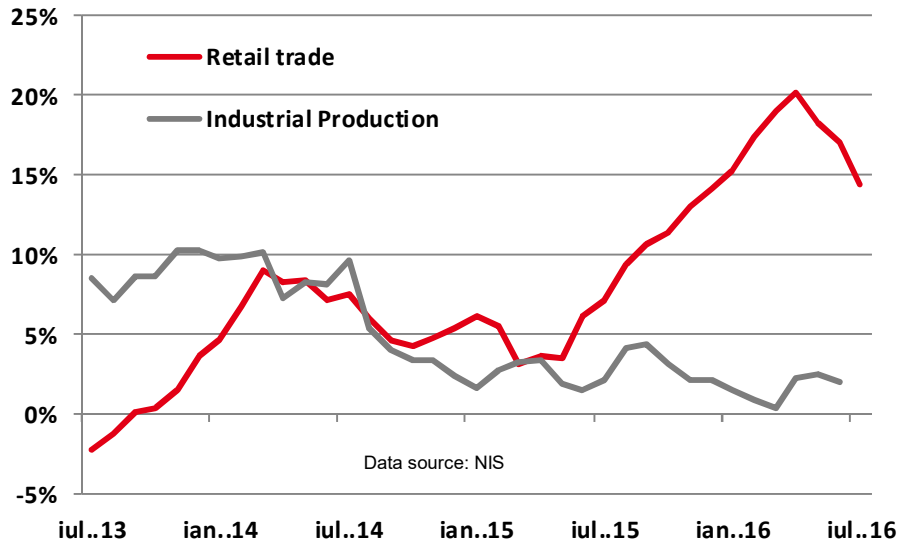
Data source: NIS



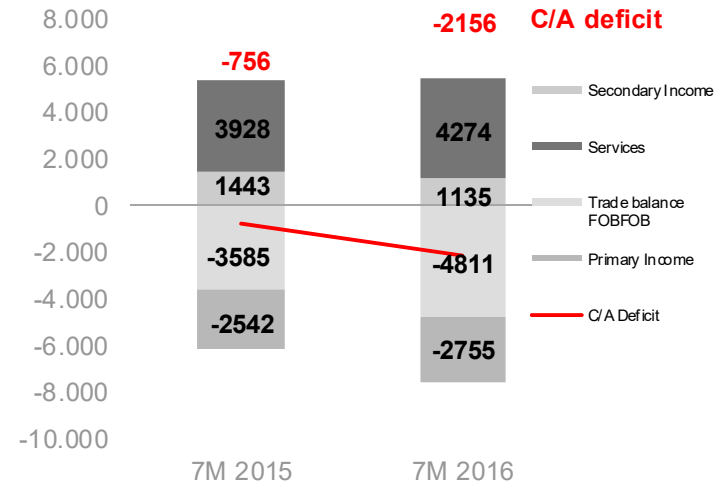
# Industrial production is trailing behind personal consumption due to limited external pull factors

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Ind Production vs. Ret Sales



Capital Inflows

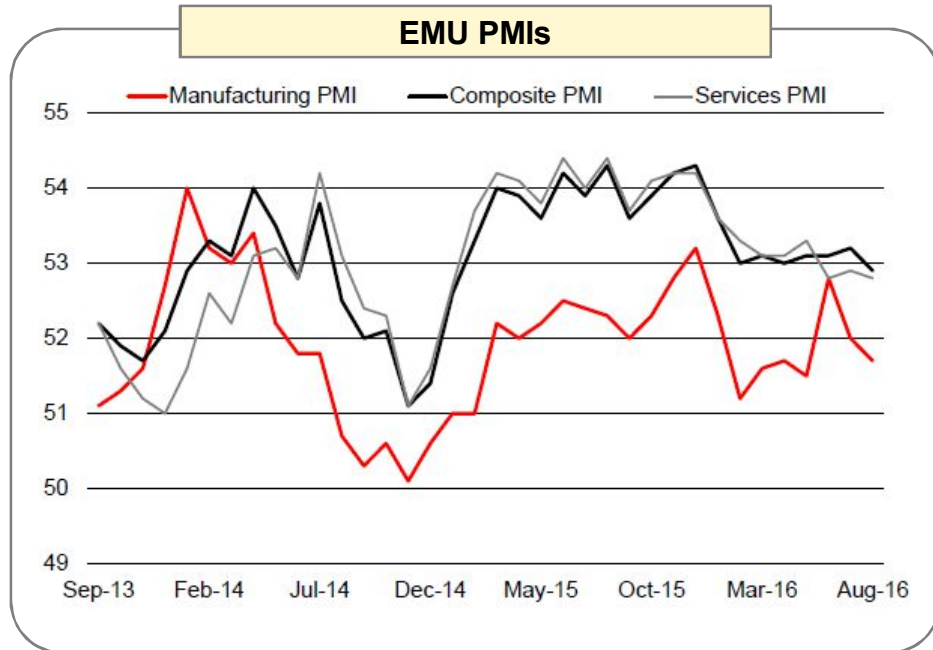


- Industrial production has been trailing behind** consumer spending due to two factors:
  - Close integration within Eurozone supply chain** has left Romania primarily as a manufacturer of **intermediate goods**. Consequently, Romanian manufacturing has been unable to capitalize on the rapid increase in consumer spending, which resulted in a sharp acceleration of imports
  - A turbulent external context** is taking a toll on the outlook for Romania's exports
- Absorption of EU funds is expected to slow down in 2016** due to a limited pipeline of projects eligible for financing under the 2014-2020 EU budget exercise. Renewed efforts from the government should improve the potential absorption for 2017
- FDI inflows have increased by 21% yoy** during the first six months of 2016, but remains at a low level (EUR 1.9mn in 6M2016)

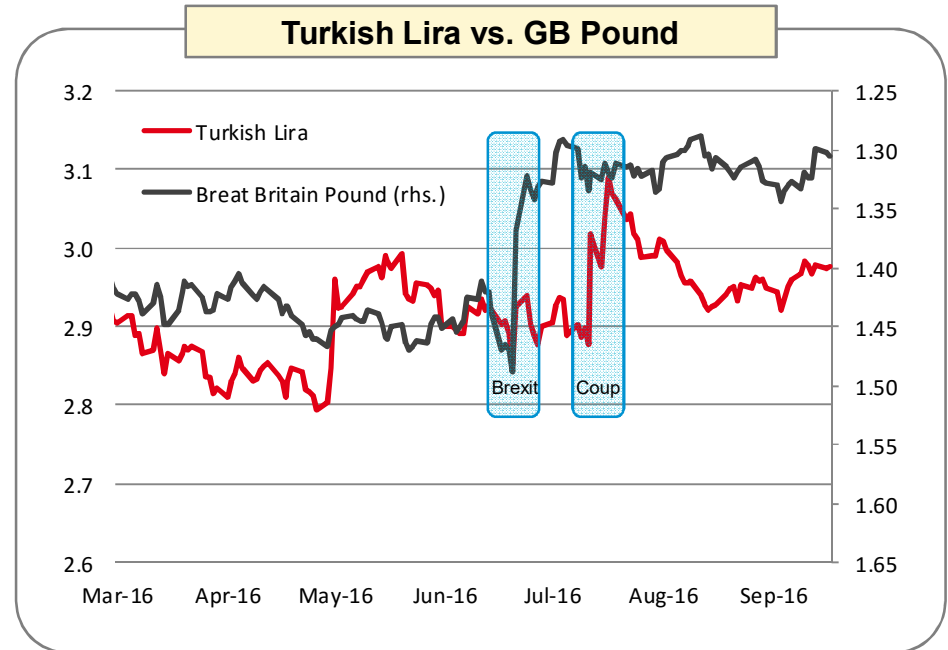


# External context remains ridden by slow growth and high uncertainty

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Data source: UniCredit Research



Data source: Reuters

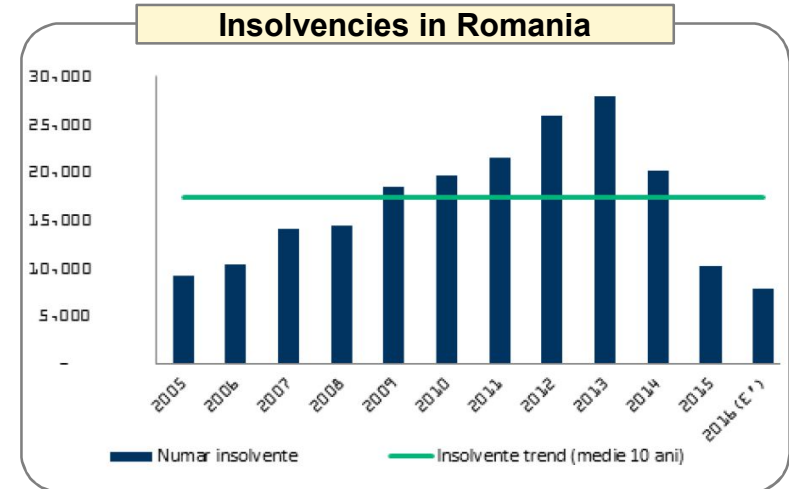
- Economic **growth in the eurozone is failing to pick up at a significant pace**. UniCredit expects the eurozone to expand by 1.6% in 2016
- **Brexit will inevitably take a toll** on the eurozone, prompting growth to slow down to 1% in 2017. Furthermore, high levels of uncertainty may plague financial markets during the negotiation phase
- **Growth in the US** has showed signs of improvement, but **momentum isn't strong enough** to prompt a tightening of the FED's monetary policy
- Weak growth dynamics should help **keep commodities at historically low prices**, particularly oil



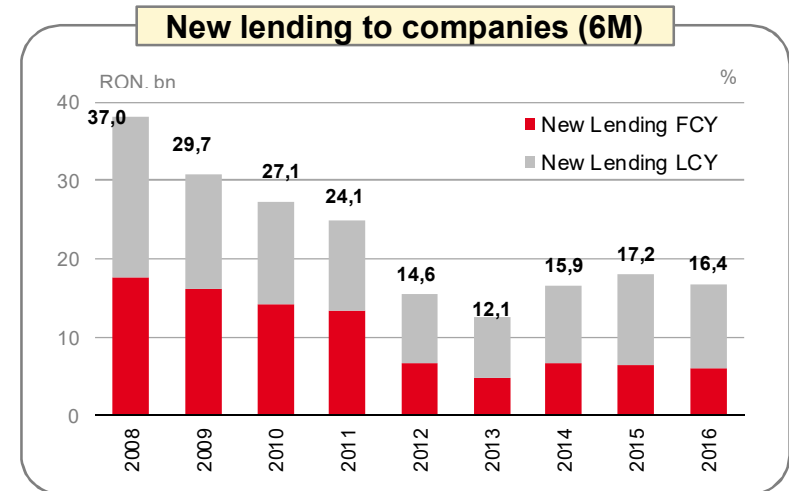
# Structural issues are holding back lending towards corporates

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- **Interest rates for lending towards companies have declined markedly** in the past years (-5.3pp for RON loans in the past 3 years), but new volumes of loans are not picking up
- The dynamic of new loans highlights **eligibility issues rather than cost issues** for corporates
  - Even though the **number of insolvencies in Romania is expected to slow** down in 2016, the country continues to record the **largest rate of insolvency in the CEE region** (23 insolvencies/1,000 active companies)
  - The level of insolvencies continues to raise **issues along the supply chain**, as local companies record **low levels of capital**
    - NBR estimates as many as **75% of loss-making companies are undercapitalized**
  - The high level of insolvencies and historically elevated NPLs make **lending towards small companies particularly risky**
  - **Large companies and multinationals generally** benefit from large **liquidity buffers** or **funding from the parent company**, which decreases appetite for new loans. The issue is compounded by monetary easing in the eurozone
- Romania recorded **68,000 newly founded companies in 1H2016** (-4.5% yoy), of which ~20% were based around Bucharest, ~14% were based in the Western region of the country and ~7% in the Eastern region



Data source: Coface

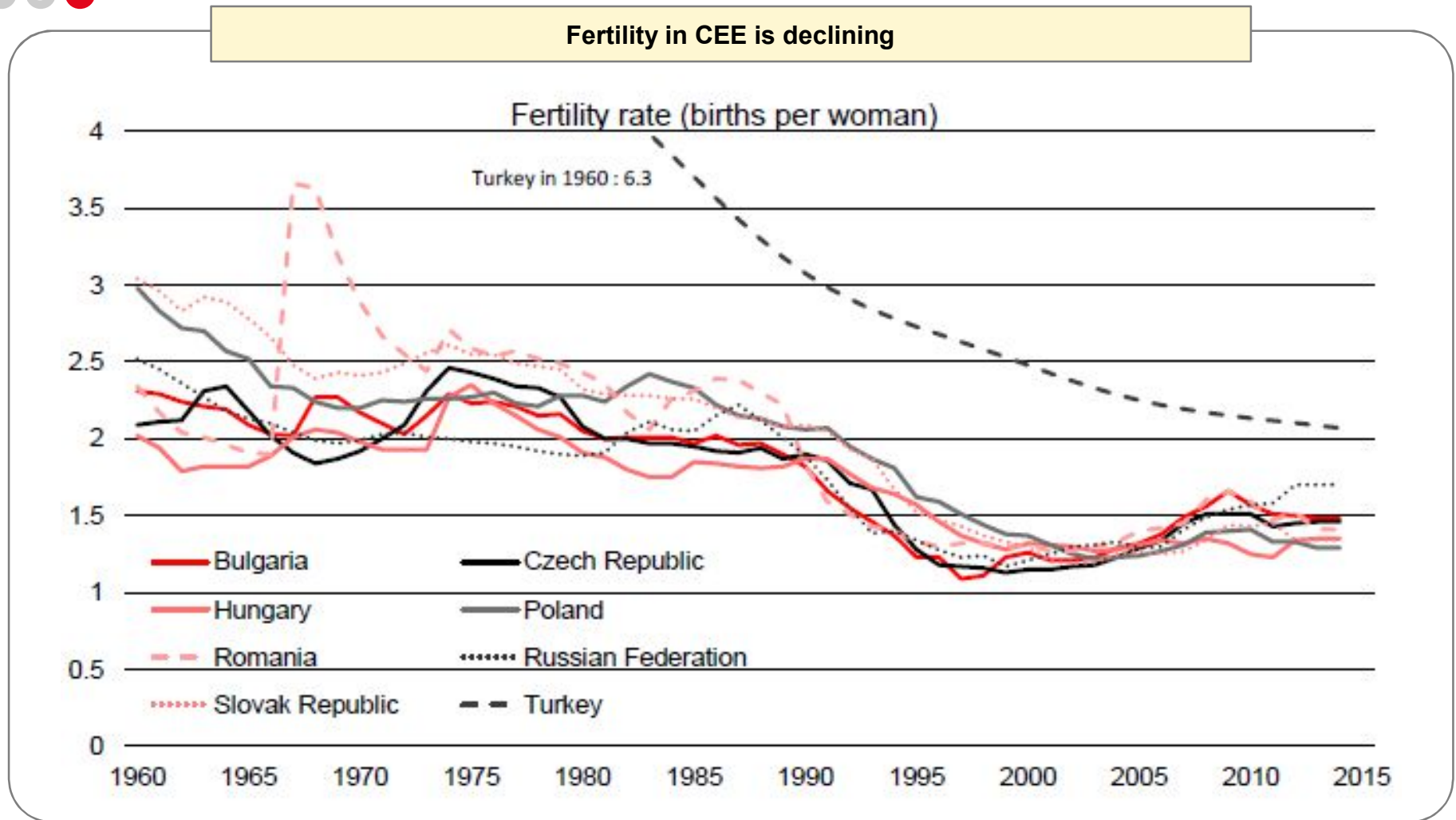


Data source: NBR



# Demographic issues are constraining the long-term growth potential

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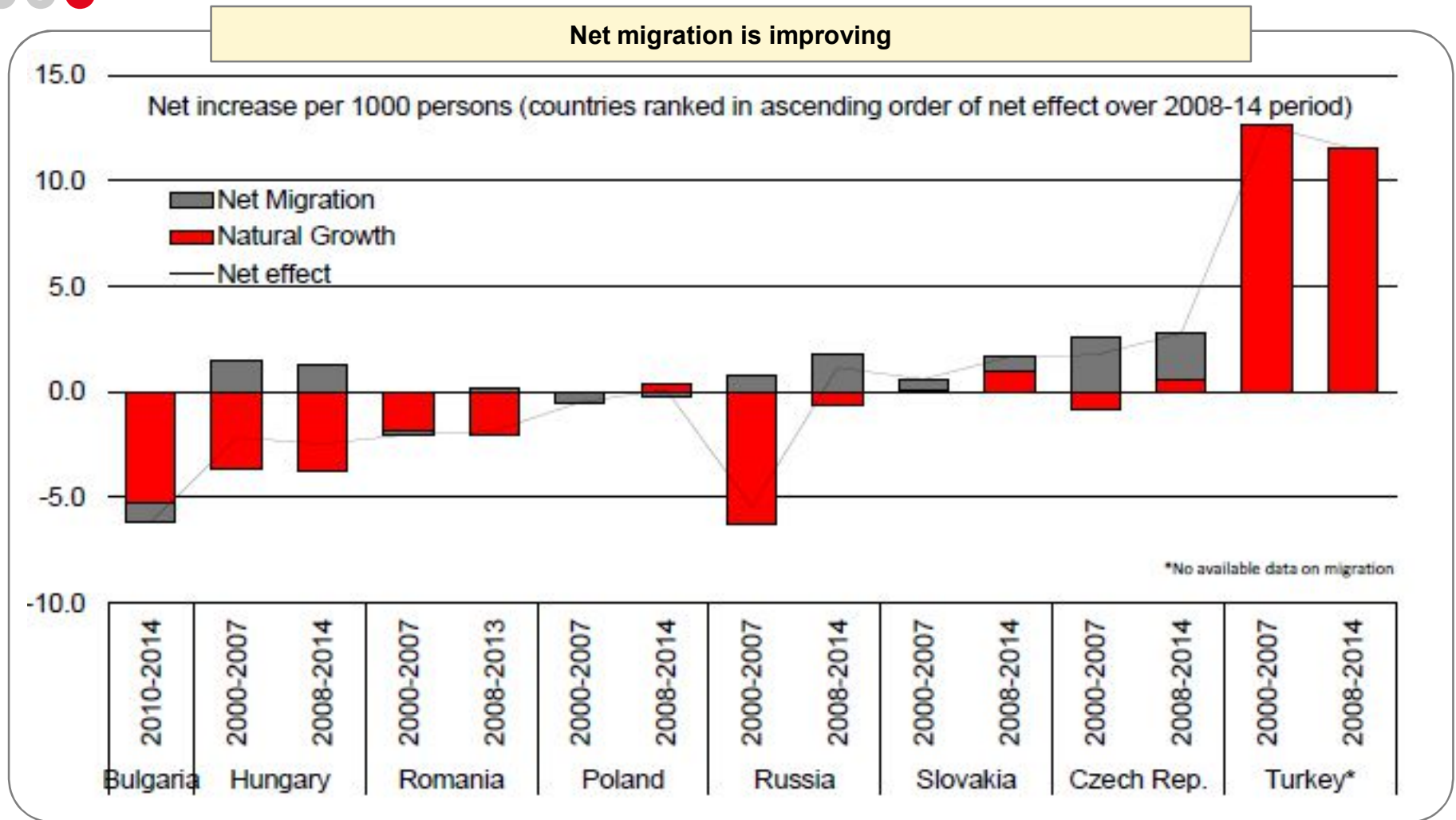


Data source: UniCredit Research



# Demographic issues are constraining the long-term growth potential

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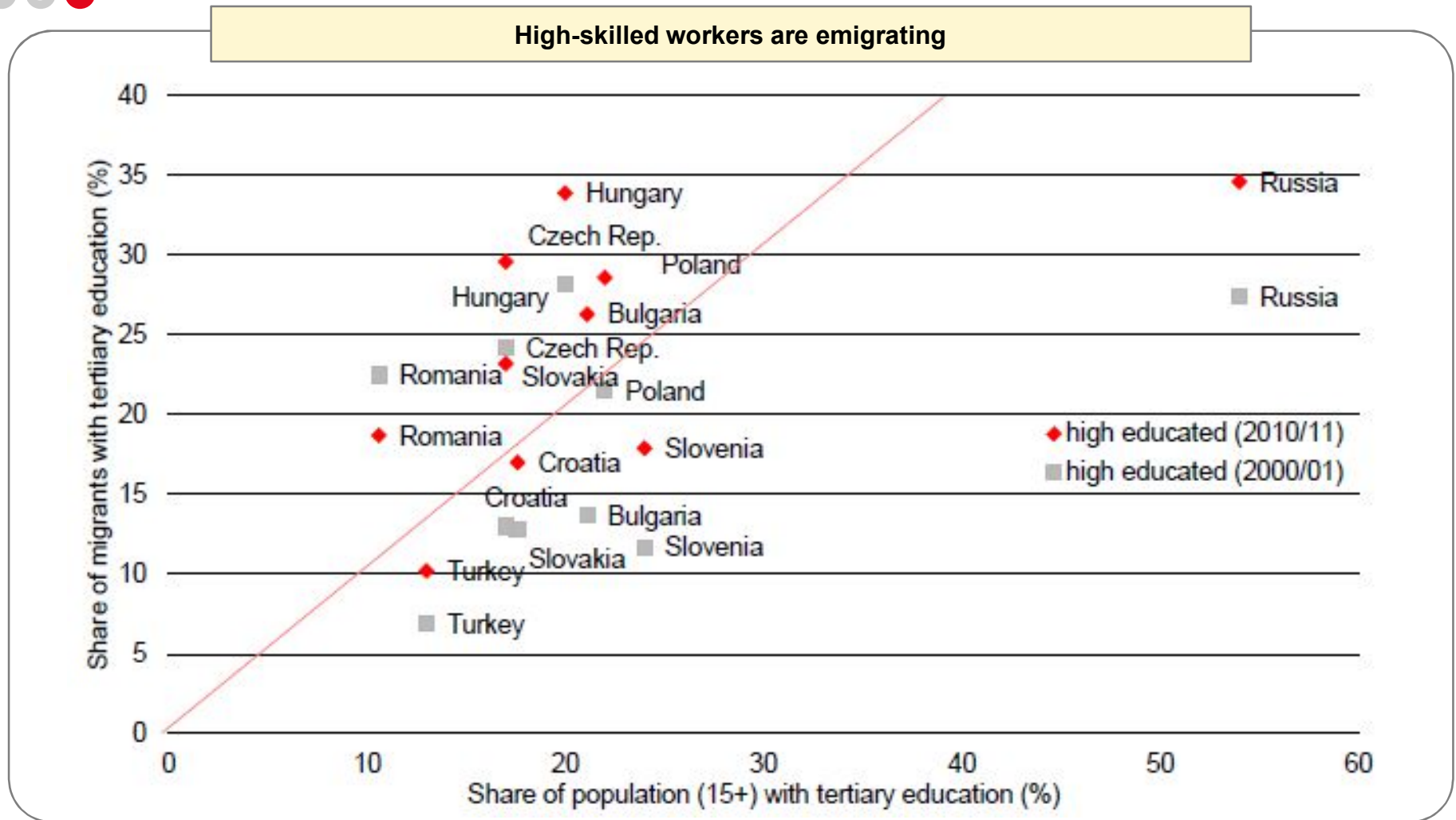


Data source: UniCredit Research



# Demographic issues are constraining the long-term growth potential

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Data source: UniCredit Research

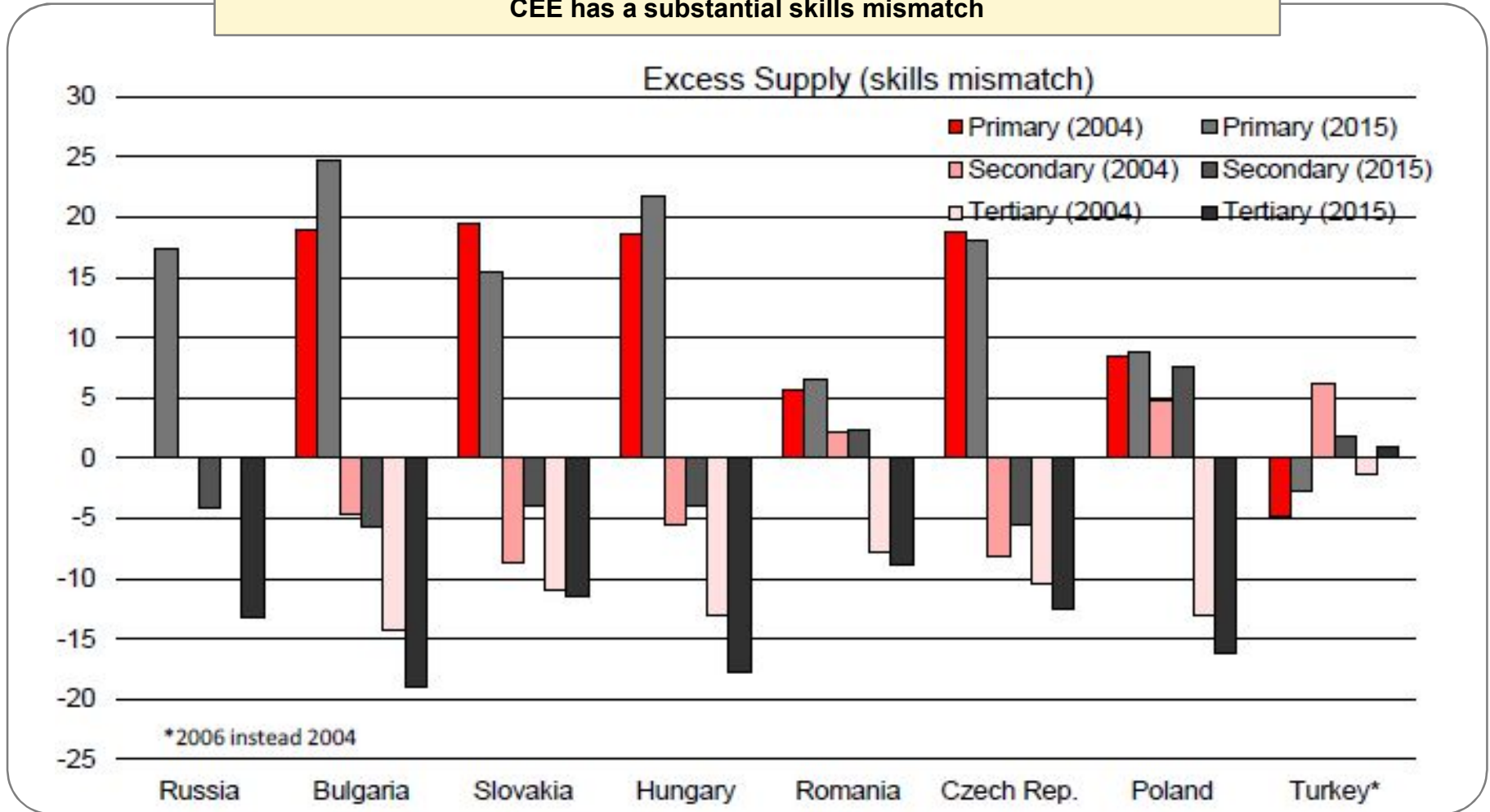




# Demographic issues are constraining the long-term growth potential

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CEE has a substantial skills mismatch



Data source: UniCredit Research

