The Romanian economy showed the first signs of recession, as GDP decreased by 0.6% in Q3 after 1.2% yoy growth observed in Q2 2012. We have downgraded our forecast of GDP growth for the second month in a row based on this data to 0.5%.

Industrial production decreased by 4.0% yoy in September despite significant progress during the month. This is also true for the major component of industrial production – manufacturing. It showed a 5.0% yoy decline despite monthly growth. As for retail trade turnover, its annual growth decelerated from 4.9% yoy in August to 2.9% yoy in September.

The consolidated general budget deficit remained constant as a share of GDP in January-September as its value increased insignificantly. The reason is austerity measures, which hinder the growth of general government expenditures. In particular, growth of the national budget was almost four times higher than that of expenditures.

Despite some deceleration in consumer inflation, it was still beyond the annual target band of 3%±1% in October at 4.96%. Growth of prices of foods once again exceeded that of prices of non-foods and services.

Both FOB exports and CIF imports decreased significantly in September. In particular, exports decreased by 9.0% yoy, while imports dropped by 8.0% yoy. Obviously, this led to further growth of commercial deficit of trade in goods, as exports decreased faster than imports. Over the first nine months of the year it grew by 3.2% yoy.

On November 7th, Romania successfully placed its new issue of benchmark bonds under the assistance of Barclays, Citigroup, Deutsche Bank, and HSBC as joint book runners. The bond was issued at a 5.04% yield. The issue showed high interest in Romanian debt instruments on the part of investors mainly in Europe, as only 15% of the issue was purchased by investors from the rest of the world. In terms of investor type, the major interest for the issue was among fund managers, as they purchased 48% of the issued bonds.

Economic Growth

Rough estimates show that GDP of Romania decreased by 0.6% yoy in Q3 2012. Overall, GDP inched up by a mere 0.2% over the first nine months of the year. This has caused us to change our forecast of GDP growth even more than we did in our report for the previous month. Now we expect GDP to grow at maximum of 0.5% yoy in 2012.

The roller coaster situation with industrial production continued in September, as it grew by 12.2% mom after the 11.0% mom drop in August and the 2.1% mom increase in July. Once again manufacturing played a crucial role in dynamics of the indicator with 15.3% mom growth. However, the monthly increases in both
industrial production in general and manufacturing in particular were not enough to obtain growth in annual terms. Industrial production in total decreased by 4.0% yoy in September, while manufacturing dropped by 5.0% yoy. At the same time, mining and quarrying grew by 6.2% yoy over the period, while electricity, gas, steam, and air conditioning supply inched up by 0.4% yoy. Continuing economic downfall in the eurozone was the major reason for the unstable development of industry in Romania, which caused a 0.2% yoy decrease in industrial production over three quarters of the year. Once again, electricity, gas, steam, and air conditioning supply grew (by 6.8% yoy), as did mining and quarrying (by 1.0% yoy), but it was still not enough to overcome a drop in manufacturing (1.2% yoy).

Looking at industrial groupings distribution of industrial production, intermediate goods decreased most (by 9.3% yoy), while consumer non-durables and capital goods experienced slower decline (by 3.2% yoy and 2.4% yoy). At the same time, growth was registered for energy (2.3% yoy) and consumer durables (2.0% yoy) in September.

Despite the fact that retail trade turnover decreased for all the major groups of products in monthly terms in September, in annual terms retail trade still preserved positive growth dynamics. In particular, total retail trade turnover decreased by 4.9% mom but grew by 2.9% yoy in September. Fuel retail for motor vehicles in specialized shops dropped by 12.0% mom but grew by 1.7% yoy, while the sale of food, beverages, and tobacco decreased by 4.1% mom but grew by 5.8% yoy. Finally, the sale of non-food products decreased by 0.7% mom but grew by 1.6% yoy in September. In the first nine months of the year, retail trade turnover managed to generate 4.0% growth.

**Fiscal Policy**

The consolidated general budget deficit grew by a tiny EUR 0.013 bln in September and reached EUR 1.59 bln over the first nine months of the year. The general budget deficit as a share of GDP remained stable at 1.18%. Once again, one can observe improvement in both the value of the deficit and its size relative to GDP in 2012 as compared to 2011. In particular, the consolidated general budget deficit was equal to EUR 3.08 bln and 2.4% of GDP in January-September 2011.

Revenues of the general budget added 7.2% yoy over January-September 2012 to reach EUR 31.35 bln. This is 23.2% of the national GDP for the corresponding period. The growth became possible thanks to, among others, a 9.5% yoy increase in tax revenues. The highest growth was registered for income taxes, which grew by 12.3% yoy. The excise revenues grew by 8.7%, which is a bit higher than the 6.2% yoy growth observed for the value added tax revenues and 6.3% yoy growth observed for the corporate tax revenues. Local administrations managed to collect 12.4% yoy more non-tax revenues, while revenues from income and property taxes inched up by a mere 0.3% yoy. Social insurance contributions continued to decelerate as they grew by 2.4% yoy in January-September 2012, reaching reached EUR 8.5 bln, compared to 3.1% yoy in January-August and 5.3% yoy in January-July of this year. Non-tax revenues observed a 28.5% yoy increase over the first nine months of the year. Finally, amounts reimbursed by the European Union as account payments from public resources reached RON 5.0 bln (EUR 1.11 bln), increasing 31% yoy. However during September, only RON 0.3 mn (EUR 0.06 mn) was added to the amounts already reimbursed by the EU during the January-August period, as the EU blocked the reimbursement on concerns of corruption and fraud.

General government expenditures observed a much lower growth rate compared to revenues. They were 1.9% up in January-September 2012 and reached EUR 32.95 bln, which was 24.4% of GDP for the period. EU-funded project expenditures experienced the highest growth among the components of general government expenditures. They grew by 30.5% yoy over the first nine months of the year. However, this growth is significantly lower than that observed over January-August, not mentioning the January-July period (36.2% yoy and 44.2% yoy respectively), as the government is reducing financing until EU concerns are addressed. At the same time, expenditures on public debt interest payments added 25.6% yoy, which is also lower than those observed in January-August. Expenditures on goods and services grew at 7.3% yoy over the reported period. Growth of the wage bill continued to accelerate for the fourth month in a row. In particular, it reached 4.3% yoy over the nine months of 2012 compared to 3.5% yoy in January-August. At the same time, growth in investment expenditures in January-September 2012 declined down to 3.0% yoy compared to 3.3% yoy observed...
in January-August. This allowed total investment expenditures to reach EUR 4.93 bln over the first nine months of the year, which was 3.6% of GDP for the period.

**Monetary Policy**

October 2012 was characterized by some decline in consumer inflation. As the data shows, total consumer inflation decelerated to 4.96% yoy from 5.33% yoy observed in September. In particular, growth of prices of food and non-food goods decelerated from 6.91% yoy to 6.14% yoy and from 4.3% yoy to 4.04% yoy respectively, while growth of prices of services inched up from 4.79% yoy to 4.89% yoy.

Broad money (M3) declined by 0.2% mom over January-October after 0.3% growth over January-September. However, in annual terms M3 grew by 6.2%, which was higher than the 5.7% yoy observed over January-September.

After decent growth of 1.3% mom the first nine months of the year, the volume of non-government loans granted by credit institutions declined by 0.3% mom in January-October. In particular, national currency-denominated loans declined by 0.3% mom, while foreign currency-denominated loans fell by 0.3% mom when expressed in RON and by 0.4% when expressed in EUR. As a result, loans to the private sector grew by 4.1% yoy over the first ten months of the year on the shoulders of 4.7% yoy growth in national currency-denominated loans and a 3.8% yoy increase in foreign currency-denominated loans (when expressed in EUR, they actually dropped by 1.1% yoy).

**International Trade and Capital**

The preliminary estimates of the National Institute of Statistics of Romania registered a 9.0% yoy decrease in FOB exports of goods in September after a 0.6% yoy increase in August. At the same time, CIF imports of goods decreased by 8.0% yoy in September, while in August they grew by 3.3% yoy. FOB exports reached EUR 3.8 bln in September 2012 and CIF imports amounted to EUR 4.6 bln. As the decline in imports was smaller than the decline in exports, the commercial deficit of trade in goods reached EUR 0.81 bln in September, which was almost 12% yoy growth. Overall, the commercial deficit of trade in goods reached EUR 7.1 bln over three quarters of 2012. This is a 3.2% increase compared to the commercial deficit of trade in goods in the first nine months of 2011.

The share of exports from Romania to the EU Member States remained almost stable at the end of September compared to that observed over the first eight months of the year (70.4% against 70.3%). At the same time, the share of imports from EU Member States to Romania increased to 73.4% at the end of September, while a month ago it was registered at 70.9%.

The current account deficit expanded over September by 18.39% to EUR 3.67 bln from EUR 3.1 bln observed over the first eight months of the year. However, in annual terms it continued decreasing at a stable rate (23.2% over January-September compared to 23.0% over January-August). Such positive dynamics became possible thanks to a decrease in the income account deficit by EUR 624 mln and an increase in the surplus of both current transfers and services (by EUR 381 mln and EUR 320 mln).

Foreign direct investments continued to grow in September but at a slower rate compared to August. In particular, FDI reached EUR 1.109 bln in January-September 2012, which is a 17.85% mom and 28.8% yoy increase. However, since the current account deficit also grew significantly, the level of its coverage with the FDI did not improve significantly (it is...
equal to 30.2% compared to 30.1% a month ago).

Medium- and long-term external debt inched up in September to EUR 77.51 bln but remained below the level observed in July. The share of medium- and long-term external debt in total external debt decreased to 78.2%. As for short-term external debt, it grew in both value and share of total debt. In particular, its value grew from EUR 20.77 bln at the end of August to EUR 21.57 bln at the end of September, which is 3.85% growth. The share of short-term external debt in total external debt inched up by 0.6% to 21.8%. From the beginning of the year, however, short-term external debt narrowed by 5.4%, while medium- and long-term debt expanded by 2.1%.

The foreign exchange reserves of Romania shrank to EUR 31.77 bln by October 31st from EUR 32.43 bln observed on September 30th. The inflows of foreign exchange amounted to EUR 2.271 bln during the month and mainly represented changes in the foreign exchange reserve requirements of credit institutions, inflows to the accounts of the Ministry of Public Finance of Romania, and income from management of foreign exchange reserves. At the same time, outflows from the foreign exchange reserves of the country amounted to EUR 2.928 bln in October and mainly represented changes in the foreign exchange reserve requirements of the credit institutions and payments of both interest and principal on foreign currency public debt. The stock of gold remained stable in terms of weight at 103.7 tonnes but its value decreased by EUR 173 mln due to negative fluctuations of the international price of gold. Total international reserves reached EUR 36.177 bln on October 31st, which was a 2.25% decrease from the value registered on September 30th.

**Other developments affecting investment climate**

On November 7th, Romania issued benchmark bonds worth EUR 1.5 bln with a 4.875% coupon and maturity in November 2019. The deal was priced at MS+370 bps (yield of 5.04%), inside the initial price guidance of MS+375 bps. Barclays, Citigroup, Deutsche Bank, and HSBC acted as joint bookrunners for the issue. The orderbook grew quickly, driven by strong demand across Europe, and reached an impressive EUR 4.7 bln, across 285 quality investors. The notable size and quality of the orderbook allowed the issuer to raise the issue premium to 20bps.

The issue is a very good result for Romania, taking into account the economic situation in the country and in the Eurozone. The issue ensures the 7-year yield of 6 bps inside the pricing of the recent 2018 tap in September on a yield basis. At the same time it provides a one-year maturity extension compared to the mentioned tap, it is larger and provides mid swap benchmark levels a bit wider.

Geographic distribution of the issue is broad: 27% of the stake was sold to Austria/Germany, 23% to the UK, 35% to the rest of Europe, 10% to US Offshore, and 5% to Asia and others. As for distribution by investor type, fund managers signed for almost half of the issue (48%), while banks and retail investors purchased 22%, insurance companies and pension funds accounted for 17%, and hedge funds purchased the remaining 13%.