



COUNTRIES IN FOCUS:

Cyprus & Romania

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Banks' profits surge, on higher net interest income

The repricing of banks' excess liquidity placed with the ECB and loan portfolio boosted net interest income

Reflecting challenges from the higher inflation and interest rate environment, the cost of risk has started to climb from historic lows, despite improving asset quality metrics

Higher provisioning needs to weigh on profitability in the period ahead

ROMANIA 2

Romanian economy is seen stalling in H2:23

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Emerging Markets Analysis

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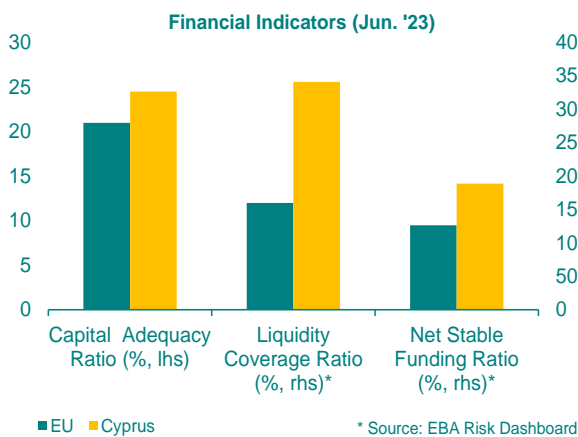
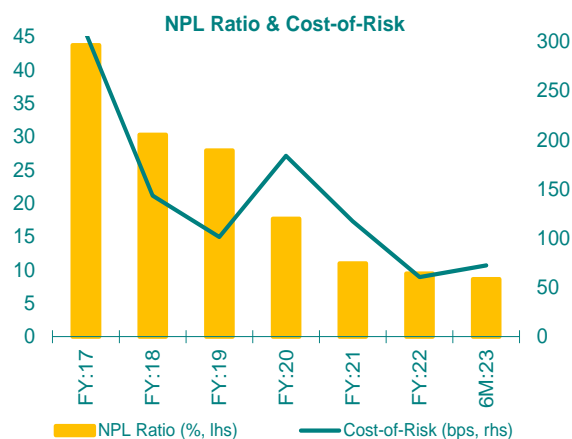
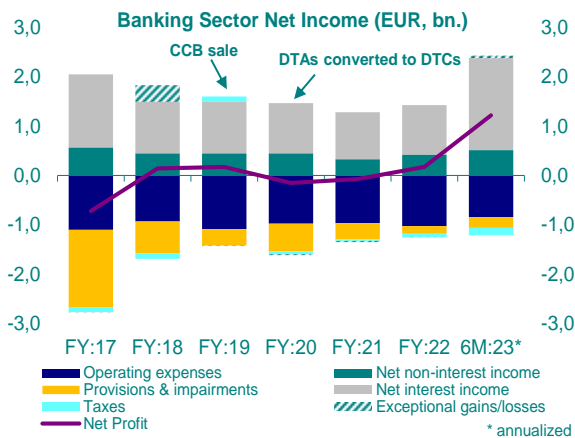
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Cyprus

BBB / Baa2 / BBB (S&P / Moody's / Fitch)



	27 Nov.	3-M F	6-M F	12-M F
1-M EURIBOR (%)	3.9	4.1	4.1	3.8
EUR/USD	1.10	1.09	1.09	1.10
Sov. Spread (2028, bps)	103	100	97	93

	27 Nov.	1-W %	YTD %	2-Y %
CSE 100	132	3.4	47.6	99.9

	2021	2022	2023F	2024F	2025F
Real GDP Growth (%)	9.9	5.1	2.5	2.5	3.0
Inflation (eop, %)	4.8	7.9	3.5	2.3	2.0
Cur. Acct. Bal. (% GDP)	-6.1	-7.9	-7.5	-6.1	-5.3
Fiscal Bal. (% GDP)	-1.9	2.4	2.2	2.2	2.0

Sources: Reuters, CBC, EBA & NBG estimates

Banks' profits surge, on higher net interest income (NII). Cypriot banks' saw a tenfold increase in their profits to EUR 1.0bn in H1:23, with (annualized) ROAE and ROAA rebounding to 29.9% and 2.6%, respectively -- much higher than the EU average of 10.8% and 0.7% -- from 2.6% and 0.2% in H1:22.

The repricing of banks' excess liquidity placed with the ECB and loan portfolio boosted NII. Amid rising interest rates, NII (accounting for c. $\frac{3}{4}$ ths of gross operating income) more than doubled in H1:23, following the repricing of banks' assets, especially placements with the ECB (accounting for 37.5% of the system's assets), and, to a lesser extent, loans to customers (with 95% of debt contracts having variable rate). Indeed, NIM surged to 286 bps in H1:23 -- well above the EU average of 160 bps -- from 140 bps in H1:22.

On the other hand, operating expenses (adjusted for Russia's RCB closure in March '22) are estimated to have risen in H1:23, but modestly, as the impact of higher inflation was moderated by that of reduced personnel, following implementation of voluntary exit schemes. Still, banks' efficiency improved sharply in H1:23, with cost-to-income ratio falling to 35.3%, well below the EU average (c. 56.5%).

Reflecting challenges from the higher inflation and interest rate environment, the cost of risk has started to climb from historic lows, despite improving asset quality metrics. Against the backdrop of rising credit risk (see also below), banks raised impairment charges in H1:23 (up 67% y-o-y, albeit from a very low base), with the cost of risk jumping to 90 bps from 49 bps in H1:22. Note that the NPL ratio moderated further to 8.7% in June from 11.2% a year ago, thanks, *inter alia*, to continuing NPL deleveraging (accounting for c. 50% of the reduction). Still, Cyprus' NPL ratio remains substantially higher than in the EU (1.6%), highlighting the poor quality of remaining NPLs, a legacy from the 2012-13 crisis, with the NPL coverage ratio standing at c. 35.0%, at the same time, below the EU average (43.0%).

Higher provisioning needs to weigh on profitability in the period ahead. The high -- yet reducing -- private sector's indebtedness (c. 175% of GDP, excl. SPEs, a significant part of which represents NPEs outside banks), together with expectations for tighter-for-longer financing conditions, mean that banks cannot but accelerate provisioning over the forecast horizon, especially in view of the high share of stage 2 loans (over 11.0% of gross loans, largely concentrated in tourism). Note that the upcoming launch of a mortgage-to-rent scheme, operated by the state-owned AMC, KEDIPEs, is set to address some of the legacy NPEs.

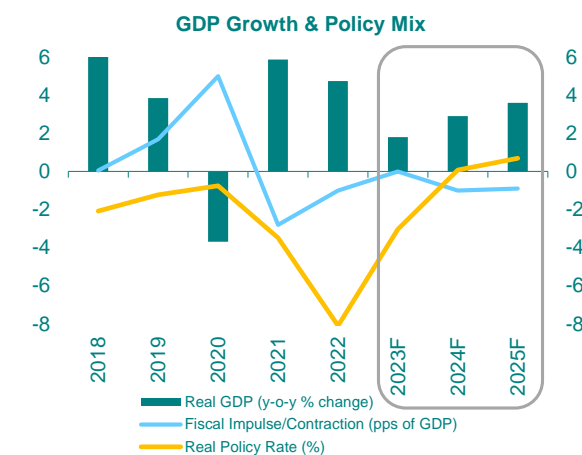
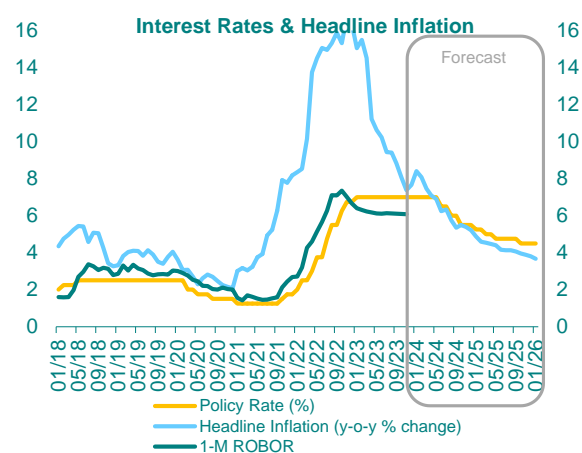
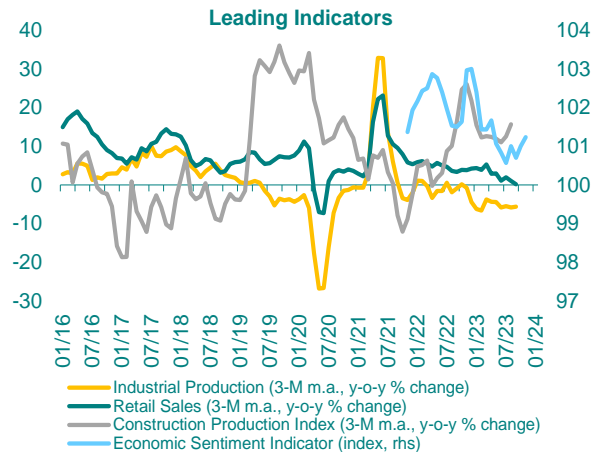
At the same time, with interest rates close or at their peak, NII should continue growing, albeit at a much slower pace than before, in line, *inter alia*, with slowing credit uptake. Importantly, reflecting banks' abundant liquidity (dominated by a low-cost deposits), NIM is expected to be sluggishly adjusted, even when rates start to fall.

Importantly, Cypriot banks are well positioned to deal with unfolding pressures, being highly-liquid, stably funded (see chart) and well-capitalised (with a total CAR of 23.3%, c. 90% of which constitutes CET1 capital). The hike in the countercyclical buffer (to 0.5% from 0% -- effective as of November '23) should further strengthen banks' resilience yet affect their appetite to provide credit.

Consolidation in the banking sector is continuing with Greece's Eurobank (parent of Eurobank Cyprus) increasing its stake in Hellenic Bank (to 55.3%). Eurobank will now have to proceed with a mandatory tender offer to minority shareholders. Assuming the deal is completed, the new merged entity will become the island's biggest lender (controlling 44% of the system's assets followed by Bank of Cyprus with 40%).

Romania

BBB- / Baa3 / BBB- (S&P / Moody's / Fitch)



	27 Nov.	3-M F	6-M F	12-M F
1-M ROBOR(%)	6.1	6.1	6.1	5.7
RON/EUR	4.97	4.98	5.00	5.02
Sov. Spread (2027, bps)	229	235	220	200

	27 Nov.	1-W %	YTD %	2-Y %
BET-BK	2,753	-0.3	25.0	14.1

	2021	2022	2023F	2024F	2025F
Real GDP Growth (%)	5.7	4.7	1.8	2.9	3.6
Inflation (eop, %)	8.2	16.4	7.7	5.2	3.8
Cur. Acct. Bal. (% GDP)	-7.2	-9.1	-6.7	-6.0	-5.6
Fiscal Bal. (% GDP)	-6.7	-5.7	-5.7	-4.7	-3.8

Sources: Reuters, INSSE, BNRO, Ministry of Finance & NBG estimates

Romanian economy is seen stalling in H2:23. The Q3:23 GDP growth flash estimate came in at 0.4% q-o-q s.a., down from 1.3% in Q2:23, with the annual pace of economic expansion easing to a meagre 0.2%, at the same time, from 1.0% in Q2:23. Although a full breakdown is not yet available, we expect the slowdown to have been driven by private consumption. Indeed, with elevated and sticky inflation constraining real disposable incomes, retail sales have been disappointing recently (see chart). Importantly, fixed investment (mostly in EU-funded public infrastructure projects, and to a lesser extent, ICT equipment) is estimated to have continued to expand at a robust pace in Q3:23, providing some counterbalancing support to GDP growth. At the same time, despite weakening external demand from the EU (as reflected, *inter alia*, by the contraction in industrial production), net exports are estimated to have marginally contributed to overall growth, due to softer domestic demand. All said, amid sluggishly improving sentiment, it is hard to expect a significant uptick in sequential GDP growth over the last quarter of the year, as the lagged impact of monetary tightening continues to feed through the economy. As a result, we see FY:23 GDP growth at 1.8%, down from 4.7% in FY:22, in line with the regional average, but well above that of the EU (up 0.4%).

Easing inflation should provide some tailwind to GDP growth in FY:24, with (EU-funded) fixed investment remaining the main contributor. Assuming inflation remains on its (slow) downward path, allowing the NBR to ease its (already relatively dovish) stance (with the first policy rate cut expected in mid-2024), private consumption should progressively gain steam, underpinned by tight labour market conditions. Still, (mostly EU-funded) public investment should remain the main driver of economic growth over the forecast horizon. Unsurprisingly, stronger domestic demand should feed into imports, resulting into net exports shaving a larger chunk off GDP growth. Note that fiscal consolidation is set to restart next year (see below), restraining economic recovery. All said, we see GDP firming to 2.9% in FY:24, below the economy's long-term potential (c. 3.5%). Economic growth could be hampered in the event distortions in global energy supply and geopolitical uncertainties translate into renewed price pressures. On the other hand, should next year's heavy election calendar (with legislative, presidential, local and EU elections due to take place) affect fiscal discipline, slowing down the pace of adjustment, GDP growth could come in higher than projected.

Fiscal rebalancing to regain pace in 2024, with the budget deficit unlikely to fall below the 3.0% of GDP mark earlier than in 2026.

The FY:23 cash budget deficit is projected at slightly below 6.0% of GDP, broadly unchanged compared with the FY:22 and well above the initial target of 4.4%, reflecting slowing growth in tax revenue, especially indirect taxes, due to weakening economic activity, and budget rigidities. Fiscal consolidation should resume only next year, when a series of measures, including a turnover tax for banks and large companies, a new tax regime for SMEs and the elimination of several tax exemptions, would be put into effect. The measures are projected to yield c. 1.2% of GDP, helping to bring the deficit down to 4.7% of GDP.

Note that Romania is the only EU state currently under the EC's Excessive Deficit Procedure. Although the bloc's fiscal rules are still not fully functional, further fiscal consolidation is critical for Romania to continue receiving RRF funds (c. EUR 29bn by 2027). Still, the budget deficit is unlikely to fall below the 3.0% of GDP mark earlier than 2026.

Importantly, public debt is set to remain in check, at the same time, hovering below 50% of GDP, with strong -- yet decelerating -- nominal GDP growth largely compensating for the impact of high budget deficits.

DETAILED MACROECONOMIC DATA

CYPRUS					
	2021	2022	2023f	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	24,928	27,777	29,566	31,184	32,800
GDP per capita (EUR)	27.687	30.516	32.128	33,550	34,940
GDP growth (real, %)	9.9	5.1	2.5	2.5	3.0
Unemployment rate (% aop)	7.5	6.8	6.3	6.0	5.7
Prices and Banking					
Inflation (% eop)	4.8	7.9	3.5	2.3	2.0
Inflation (% aop)	2.4	8.4	3.8	2.9	2.1
Loans to the Private Sector (% change, eop)	-5.0	-12.1			
Customer Deposits (% change, eop)	5.4	2.8			
Loans to the Private Sector (% of GDP)	110.1	86.8			
Retail Loans (% of GDP)	49.0	41.4			
Corporate Loans (% of GDP)	61.1	45.4			
Customer Deposits (% of GDP)	174.1	160.7			
Loans to Private Sector (% of Deposits)	63.2	54.0			
Foreign Currency Loans (% of Total Loans)	---	---			
External Accounts					
Merchandise exports (EUR million)	3,693	4,581	4,651	4,811	4,935
Merchandise imports (EUR million)	8,092	10,555	11,093	11,431	11,794
Trade balance (EUR million)	-4,398	-5,973	-6,442	-6,620	-6,859
Trade balance (% of GDP)	-17.6	-21.5	-21.8	-21.2	-20.9
Current account balance (EUR million)	-1,514	-2,203	-2,209	-1,916	-1,735
Current account balance (% of GDP)	-6.1	-7.9	-7.5	-6.1	-5.3
Net FDI (EUR million)	7,748	8,446	10,768	13,460	16,825
Net FDI (% of GDP)	31.1	30.4	36.4	43.2	51.3
International reserves (EUR million)	---	---	---	---	---
International reserves (Months ^a)	---	---	---	---	---
Public Finance					
Primary balance ^b (% of GDP)	-0.1	3.9	3.6	3.5	3.4
Fiscal balance ^b (% of GDP)	-1.9	2.4	2.2	2.2	2.0
Gross public debt (% of GDP)	99.3	85.6	81.5	75.2	69.5
External Debt					
Gross external debt (EUR million)	172,529	169,326	168,326	166,826	165,326
Gross external debt (% of GDP)	692.1	609.6	569.3	535.0	504.0
External debt service (EUR million)	---	---	---	---	---
External debt service (% of reserves)	---	---	---	---	---
External debt service (% of exports)	---	---	---	---	---
Financial Markets					
Policy rate (ECB refinancing rate, % eop)	0.0	2.5	4.5	4.3	3.5
Policy rate (ECB refinancing rate, % aop)	0.0	0.7	3.8	4.4	4.0
10-Y T-bond rate (% eop)	0.7	4.2	3.8	3.8	3.7
Exchange rate: USD (eop)	1.137	1.070	1.090	1.100	1.120
Exchange rate: USD (aop)	1.183	1.053	1.080	1.095	1.110

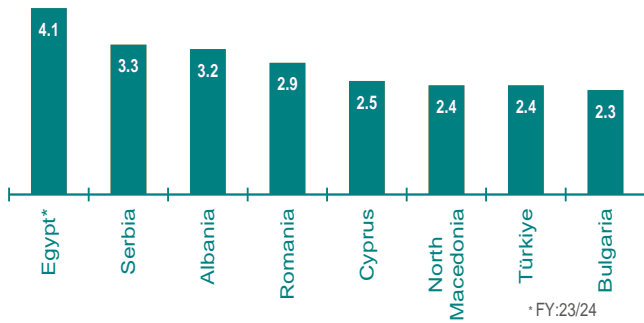
f: NBG forecasts; a: months of imports of GNFS; b: cash basis

ROMANIA					
	2021	2022	2023f	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	241,737	286,097	320,664	347,897	372,948
GDP per capita (EUR)	12,589	15,025	17,030	18,634	20,151
GDP growth (real, %)	5.7	4.7	1.8	2.9	3.6
Unemployment rate(ILO definition, %, aop)	5.6	5.6	5.5	5.5	5.3
Prices and Banking					
Inflation (% eop)	8.2	16.4	7.7	5.2	3.8
Inflation (% aop)	5.0	13.7	10.6	6.5	4.2
Loans to the Private Sector (% change, eop)	14.3	11.2			
Customer Deposits (% change, eop)	13.7	6.7			
Loans to the Private Sector (% of GDP)	26.3	24.7			
Retail Loans (% of GDP)	13.8	12.1			
Corporate Loans (% of GDP)	12.5	12.5			
Customer Deposits (% of GDP)	38.7	34.7			
Loans to Private Sector (% of Deposits)	68.0	71.1			
Foreign Currency Loans (% of Total Loans)	26.5	29.9			
External Accounts					
Merchandise exports (EUR million)	70,194	86,015	87,280	92,145	96,990
Merchandise imports (EUR million)	93,317	118,065	116,323	122,571	129,136
Trade balance (EUR million)	-23,123	-32,050	-29,043	-30,426	-32,146
Trade balance (% of GDP)	-9.6	-11.2	-9.1	-8.7	-8.6
Current account balance (EUR million)	-17,474	-26,041	-21,496	-20,730	-20,802
Current account balance (% of GDP)	-7.2	-9.1	-6.7	-6.0	-5.6
Net FDI (EUR million)	8,820	8,808	8,368	8,577	9,006
Net FDI (% of GDP)	3.6	3.1	2.6	2.5	2.4
International reserves (EUR million)	40,475	46,636	53,258	56,105	56,809
International reserves (Months ^a)	4.3	3.9	4.5	4.5	4.5
Public Finance					
Primary balance (% of GDP)	-5.2	-3.7	-3.6	-2.7	-1.8
Fiscal balance (% of GDP)	-6.7	-5.7	-5.7	-4.7	-3.8
Gross public debt ^b (% of GDP)	48.3	47.0	47.7	48.7	49.2
External Debt					
Gross external debt (EUR million)	136,585	143,886	160,332	170,469	179,015
Gross external debt (% of GDP)	56.5	50.3	50.0	49.0	48.0
External debt service (EUR million)	16,702	19,195	18,250	18,500	18,750
External debt service (% of reserves)	41.3	41.2	34.3	33.0	31.9
External debt service (% of exports)	17.0	15.6	14.3	13.7	13.1
Financial Markets					
Policy rate (1-w repo rate, %, eop)	1.8	6.8	7.0	5.5	4.5
Policy rate (1-w repo rate, %, aop)	1.4	4.4	7.0	6.4	4.8
10-Y Bond Yield (% eop)	5.1	8.4	7.0	6.6	6.2
Exchange rate: EUR (eop)	4.946	4.940	4.980	5.020	5.050
Exchange rate: EUR (aop)	4.919	4.928	4.950	5.000	5.035

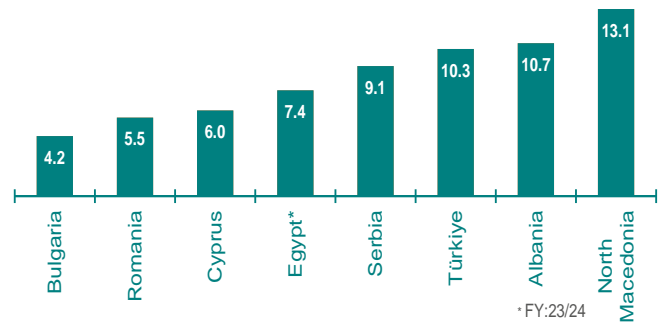
f: NBG forecasts; a: months of imports of GNFS; b: ESA 2010

REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

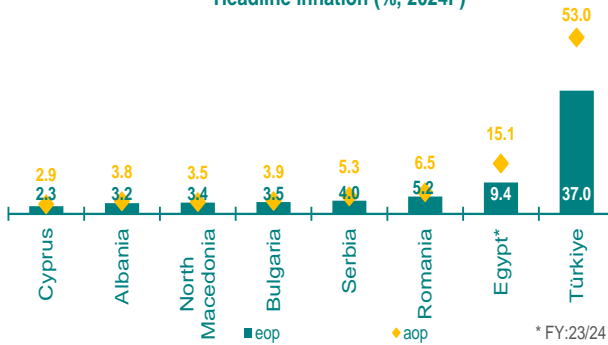
Real GDP Growth (% , 2024F)



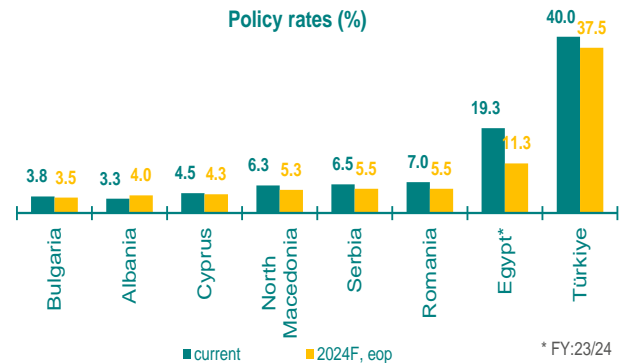
Unemployment (% , 2024F, aop)



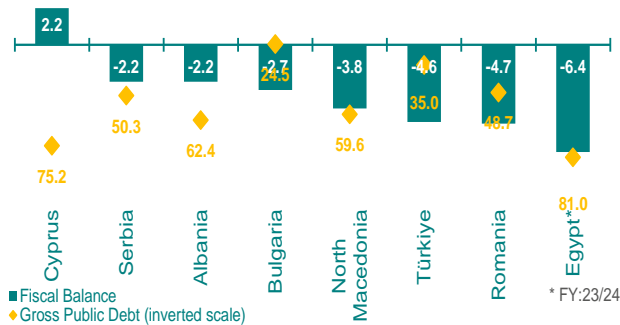
Headline inflation (% , 2024F)



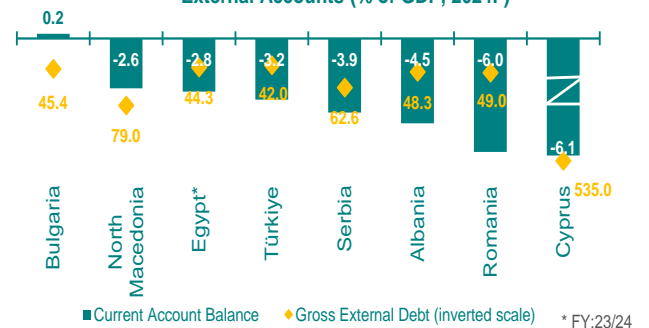
Policy rates (%)



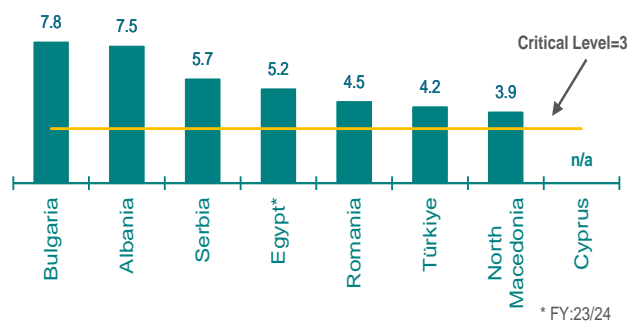
Public Finance (% of GDP, 2024F)



External Accounts (% of GDP, 2024F)

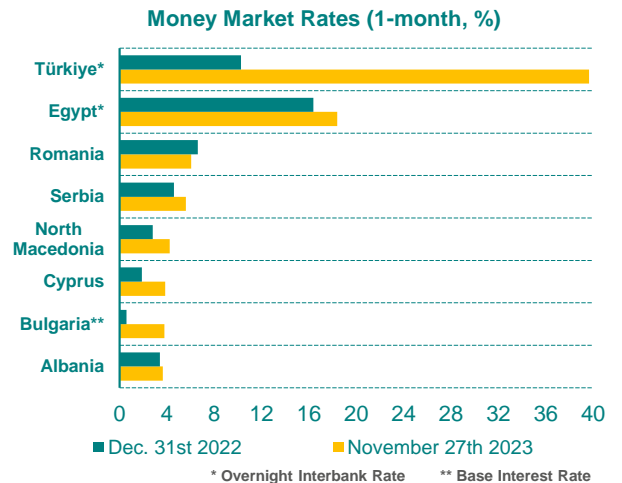
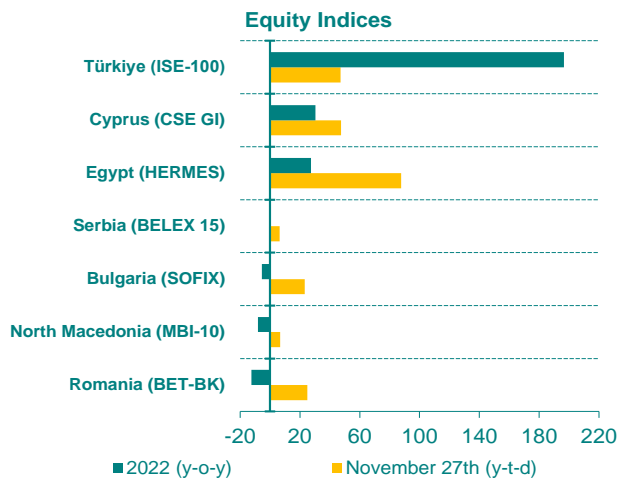
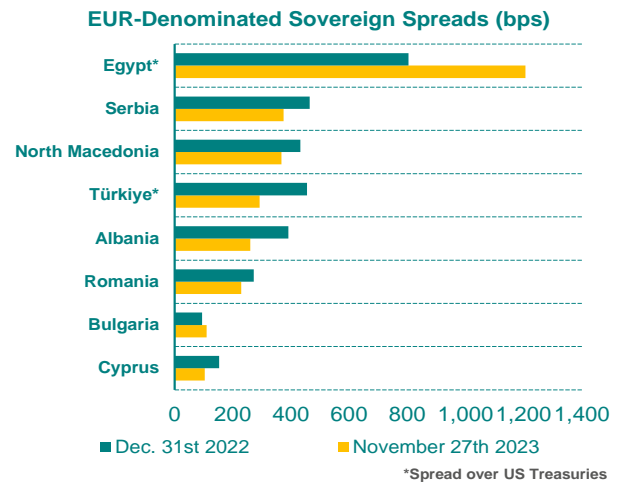
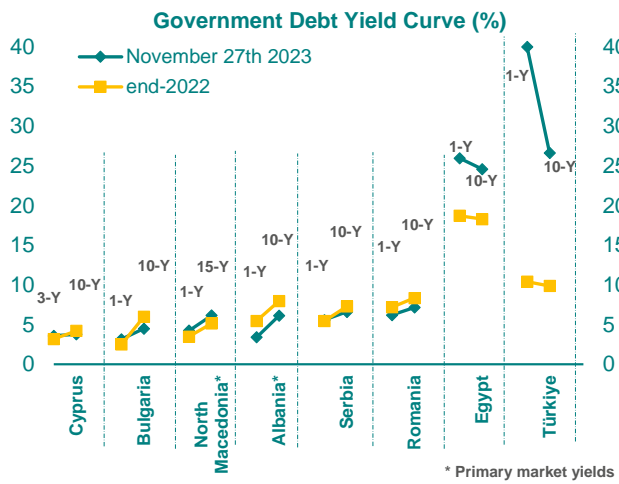
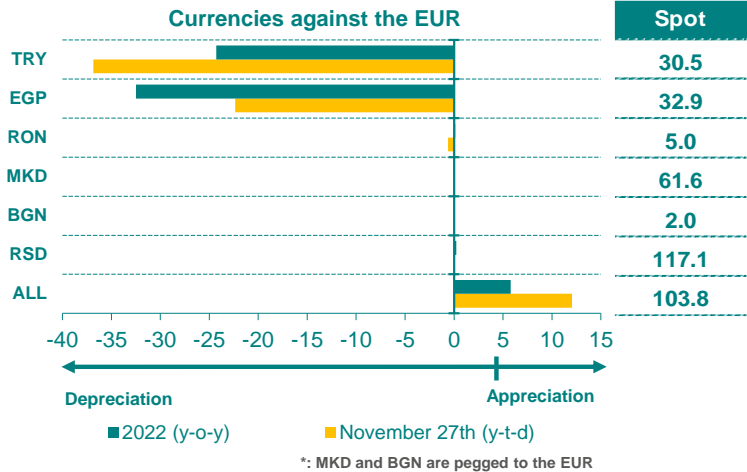


FX Reserves (Months of Imports, 2024F)



Sources: National Sources & NBG estimates

REGIONAL SNAPSHOT: FINANCIAL MARKETS



Sources: Reuters & NBG estimates

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