



## COUNTRIES IN FOCUS:

### Romania & Bulgaria

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Under the burden of still elevated inflation, tightening financing conditions and weak economic sentiment, Romania braces for a soft landing in FY:23 (GDP, up 2.8% against 4.8% in FY:22)

#### BULGARIA ..... 2

Banks' profits strengthened in FY:22, thanks to stronger net operating income, especially net interest income (NII)

NII rebounded in FY:22, on fast credit expansion and rising interest rates

Provisioning charges dropped in FY:22, reflecting improved asset quality metrics

Against a challenging economic backdrop, banking profitability should come under (modest) pressure in FY:23

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### NBG – Economic Analysis Division

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### Emerging Markets Analysis

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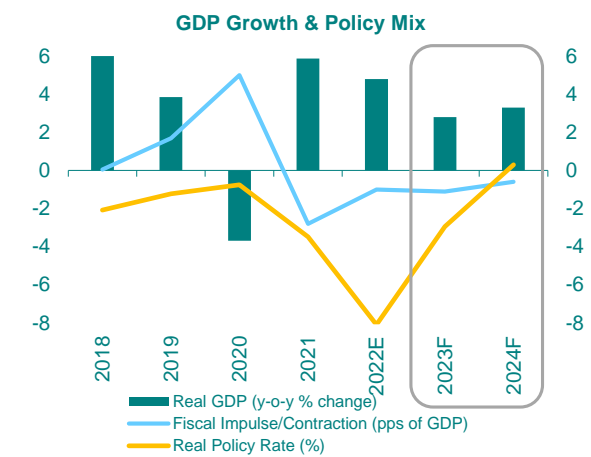
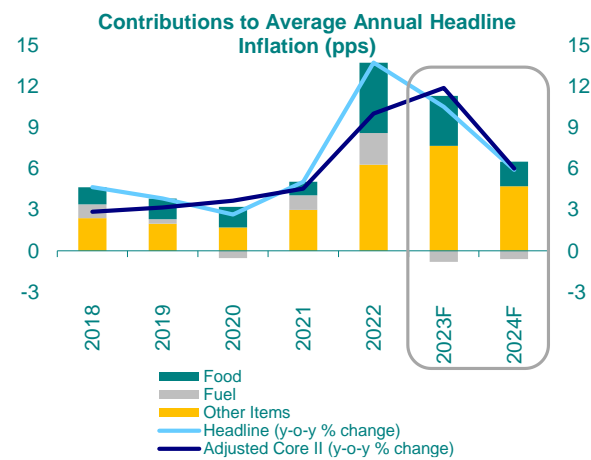
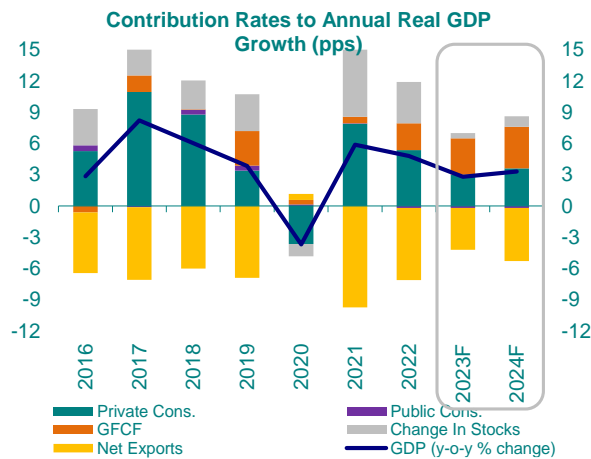
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# Romania

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



	8 May	3-M F	6-M F	12-M F
1-M ROBOR(%)	6.1	6.6	6.6	6.0
RON/EUR	4.92	4.94	4.96	4.96
Sov. Spread (2027, bps)	287	275	260	220

	8 May	1-W %	YTD %	2-Y %
BET-BK	2,322	-1.3	5.4	4.2

	2020	2021	2022E	2023F	2024F
Real GDP Growth (%)	-3.7	5.9	4.8	2.8	3.3
Inflation (eop, %)	2.1	8.2	16.4	7.7	4.3
Cur. Acct. Bal. (% GDP)	-4.9	-7.2	-9.3	-7.8	-6.8
Fiscal Bal. (% GDP)	-9.5	-6.7	-5.7	-4.6	-4.0

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

**Under the burden of still elevated inflation, tightening financing conditions and weak economic sentiment, Romania braces for a soft landing in FY:23 (GDP, up 2.8% against 4.8% in FY:22).**

Although headline inflation has likely peaked (at 15.5% y-o-y in February), it is set to remain elevated throughout the year, continuing to bite on (real) disposable income. With the precautionary savings built during the pandemic having been already exhausted, this income effect cannot but weigh on private consumption, but modestly, as still tight labour market conditions and strong wage growth (on the back, *inter alia*, of a 17.6% hike in the minimum wage) should provide a backstop.

At the same time, against the backdrop of stagnating GDP growth in the EU, net exports should remain a drag on overall growth, despite the offsetting impact of weaker private consumption and easing strains in global supply chains. In fact, the large import content of fixed investment, which is expected to overperform in the period ahead, means that imports would continue to expand at a solid pace.

Indeed, despite poor business confidence, rising interest rates and elevated construction costs, investment activity is set to progressively gain momentum, bolstered by EU funding, providing a critical contribution to GDP growth. Note that Romania is eligible to receive grants and loans worth EUR 27.1bn (or more than 9.5% of its FY:22 GDP) under the EU RRF in 2021-26 along with structural EU funds worth c. EUR 50bn (17.5% of FY:22 GDP), with the historical low EU funds absorption rate posing, however, serious challenges in this regard.

Policies are not envisaged to sustain economic growth this year. On the one hand, the need to reduce the high structural budget deficit should tie the Government's hands, despite the EU's relaxed stance on fiscal discipline rules. Note that, following a significant narrowing in the budget deficit over the past 2 years, further fiscal consolidation appears difficult to be sustained in the absence of structural reforms (especially focusing on the weak tax base, 2<sup>nd</sup> lowest in the EU), which authorities, however, appear reluctant to push with ahead of the 2024 elections.

On the other hand, in an environment of still elevated inflation and wide external imbalances (reflecting, *inter alia*, fiscal imbalances and low domestic savings), the NBR cannot but maintain a tight stance. As a result, we expect the latter to maintain its key rate at the current high of 7.0% (against 1.75% at end-2021) at least by early next year.

All said, we see GDP growth moderating to 2.8% in FY:23 -- well above the euro area average of c. 1.0% -- underpinned a significant carry-over effect (projected at 1.7 pps against 1.3 pps in the previous year). Note that domestic demand in Romania would be less affected by rising interest rates than in other EU economies, thanks to the very low lending penetration rate (standing at a mere 25.0% of GDP). Assuming that inflation loosens its grip on the economy in FY:24 and sentiment improves, we see GDP growth accelerating to 3.3%, broadly in line with the economy's long-term potential, driven by a broad-based expansion in domestic demand.

Uncertainty over the course of the war in neighbouring Ukraine and the spillover from a more substantive and disorderly tightening in global financing conditions pose downside risks to our forecast. On the upside, a faster-than-envisaged moderation in inflationary pressures could spur economic growth.

The forthcoming rotation in Government portfolios between the two coalition partners, namely the centre-left PSD and the centre-right PNL, in May should be smooth. In fact, according to the latest opinion polls, a coalition between the same partners would be the most likely outcome of next year's elections.

# Bulgaria

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

**Banks' profits strengthened in FY:22, thanks to stronger net operating income, especially net interest income (NII).** In FY:22, banks' profits surged by 46.8% to BGN 2.1bn (1.3% of GDP), with ROAE and ROAA rising further to 12.3% and 1.4% in FY:22, respectively, from 8.9% and 1.1% in FY:21.

**NII rebounded in FY:22, on fast credit expansion and rising interest rates.** Strong credit growth (up 12.2% against a rise of 8.3% in FY:21, mainly driven by the corporate segment) and the full resumption of deferred debt payments under the COVID-19 debt moratorium, boosted NII in FY:22 (up 17.0%). The widening in the net interest margin (NIM, to 227 bps in FY:22 from 218 bps in FY:21, nearly double that of euro area banks), reflecting repricing not only of loans but also of banks' large cash balances held with the central bank, amid rising interest rates, did also provide some support.

Adding to profitability, net non-interest income (NNII) also strengthened in FY:22 (up 18.6%), driven by net fees & commission income. Profitability would have been even stronger had operating expenses not surged (up 9.5%), in line with rising inflation. All said, the efficiency of the banking system improved, with the cost-to-income ratio falling to 46.3% in FY:22 from 50.3% in FY:21, much better than the EU average (c. 61%).

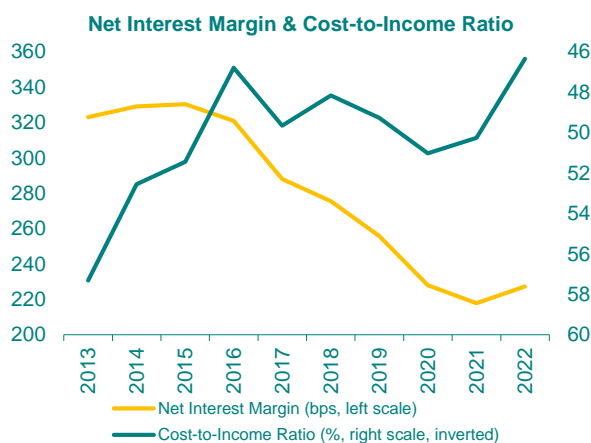
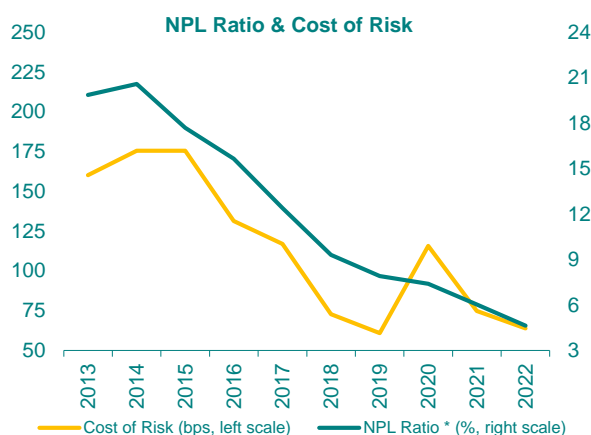
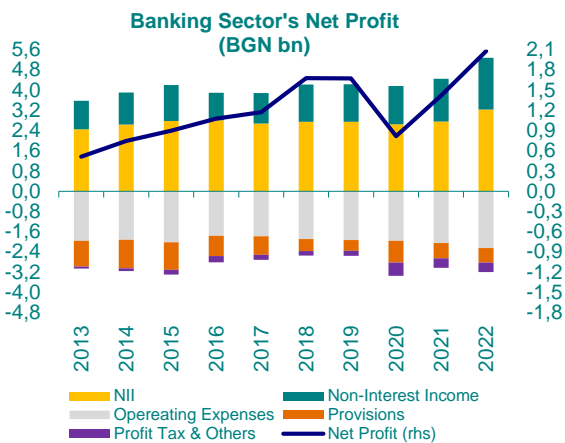
**Provisioning charges dropped in FY:22, reflecting improved asset quality metrics.** Economic recovery (together with the impact of fast credit expansion) benefitted the system's asset quality metrics, with the NPE ratio falling to a post-GFC low of 4.6% at end-2022 (still higher than that of Bulgaria's regional peers) from 6.0% at end-2021. As a result, banks continued to build up provisions in FY:21, but at a somewhat slower pace compared with the previous year, bringing the cost-of-risk further down to 64 bps from 75 bps in FY:21. Reflecting improved asset quality, the NPE coverage ratio rose to 66.5% at end-2022 from 51.3% at end-2021, well above the EU average of c. 43.0%.

**Against a challenging economic backdrop, banking profitability should come under (modest) pressure in FY:23.** Tightening financing conditions, together with slowing economic growth and heightened uncertainty, raise significant challenges to banks this year. Note that, despite abundant liquidity in the domestic banking system (with the loan-to-deposit ratio standing at just 67.6% at end-2022), Bulgaria's reference rate (BIR) has already surged to 2.8% (May '23), up from 1.3% at end-2022 and 0% a year ago.

In this environment of rising interest rates, credit uptake cannot but slow down this year (with the corporate sector remaining the main driver, due to the need to co-finance -- with the EU -- the investment projects included in the country's Recovery & Resilience Plan). The hike in the countercyclical capital buffer (to 1.5% in April 2023 from 1.0% in October 2022 and 0.5% prior to October) should also affect banks' appetite to expand their loan portfolios. Importantly, however, the impact of slower credit expansion on NII should be largely moderated by the envisaged further strengthening in the NIM.

At the same time, with households' and corporates' repayment capacity coming under growing stress, and in view of the already elevated ratio of underperforming loans (i.e. Stage 2 loans, standing at a high of more than 12.0%), banks are expected to accelerate provisioning in FY:23.

Note that banks' exposure to Government debt is relatively small (with related holding accounting for c. 15.0% of their assets, c. 2/3<sup>rds</sup> of which are classified as "held-to-maturity"), limiting downside risks from unrealized losses. In any case, banks' strong overall capital adequacy (with the associated ratio currently standing at 20.9%, c. 96% of which constitutes CET1 capital) provides headroom to absorb potential losses.



	8 May	3-M F	6-M F	12-M F
Base Interest Rate (%)	2.8	3.1	3.3	3.1
BGN/EUR	1.96	1.96	1.96	1.96
Sov. Spread (2027, bps)	145	145	135	115

	8 May	1-W %	YTD %	2-Y %
SOFIX	614	0.7	2.1	18.5

	2020	2021	2022E	2023F	2024F
Real GDP Growth (%)	-4.0	7.6	3.4	1.7	2.9
Inflation (eop, %)	0.1	7.8	16.9	5.9	3.2
Cur. Acct. Bal. (% GDP)	0.0	-1.9	-0.7	-0.4	-0.1
Fiscal Bal. (% GDP)	-2.9	-2.8	-0.8	-4.0	-3.0

Sources: Reuters, BNB, EBA & NBG estimates

## DETAILED MACROECONOMIC DATA

ROMANIA					
	2020	2021	2022	2023f	2024f
<b>Real Sector</b>					
Nominal GDP (EUR million)	220,628	241,394	286,640	324,791	353,871
GDP per capita (EUR)	11,414	12,571	14,929	16,917	18,434
GDP growth (real, %)	-3.7	5.9	4.8	2.8	3.3
Unemployment rate(ILO definition, %, aop)	6.1	5.6	5.6	5.6	5.4
<b>Prices and Banking</b>					
Inflation (% eop)	2.1	8.2	16.4	7.7	4.3
Inflation (% aop)	2.6	5.0	13.7	10.5	5.9
Loans to the Private Sector (% change, eop)	5.0	14.3	11.2		
Customer Deposits (% change, eop)	15.3	13.7	6.7		
Loans to the Private Sector (% of GDP)	25.7	26.4	24.6		
Retail Loans (% of GDP)	14.0	13.9	12.2		
Corporate Loans (% of GDP)	11.6	12.4	12.5		
Customer Deposits (% of GDP)	38.2	38.9	34.8		
Loans to Private Sector (% of Deposits)	67.3	67.8	70.8		
Foreign Currency Loans (% of Total Loans)	29.7	26.5	29.9		
<b>External Accounts</b>					
Merchandise exports (EUR million)	57,560	70,194	85,833	91,933	96,818
Merchandise imports (EUR million)	76,509	93,317	118,175	125,384	131,292
Trade balance (EUR million)	-18,949	-23,123	-32,342	-33,451	-34,475
Trade balance (% of GDP)	-8.6	-9.6	-11.3	-10.3	-9.7
Current account balance (EUR million)	-10,900	-17,474	-26,689	25,206	-24,083
Current account balance (% of GDP)	-4.9	-7.2	-9.3	-7.8	-6.8
Net FDI (EUR million)	2,960	8,820	9,626	10,107	10,815
Net FDI (% of GDP)	1.3	3.7	3.4	3.1	3.1
International reserves (EUR million)	37,379	40,475	46,636	48,288	50,769
International reserves (Months <sup>a</sup> )	4.9	4.3	3.9	3.8	3.8
<b>Public Finance</b>					
Primary balance (% of GDP)	-8.2	-5.2	-3.7	-2.5	-2.0
Fiscal balance (% of GDP)	-9.5	-6.7	-5.7	-4.6	-4.0
Gross public debt <sup>b</sup> (% of GDP)	46.5	48.3	47.0	46.7	47.1
<b>External Debt</b>					
Gross external debt (EUR million)	126,750	136,585	144,561	153,301	162,073
Gross external debt (% of GDP)	57.4	56.6	50.4	47.2	45.8
External debt service (EUR million)	17,291	16,702	19,195	18,250	18,500
External debt service (% of reserves)	46.3	41.3	41.2	37.8	36.4
External debt service (% of exports)	21.3	17.0	15.6	13.8	13.2
<b>Financial Markets</b>					
Policy rate (1-w repo rate, %, eop)	1.5	1.8	6.8	7.0	5.3
Policy rate (1-w repo rate, %, aop)	1.8	1.4	4.4	7.0	6.0
10-Y Bond Yield (% eop)	3.1	5.1	8.4	7.4	6.7
Exchange rate: EUR (eop)	4.863	4.946	4.940	4.960	4.960
Exchange rate: EUR (aop)	4.835	4.919	4.928	4.950	4.960

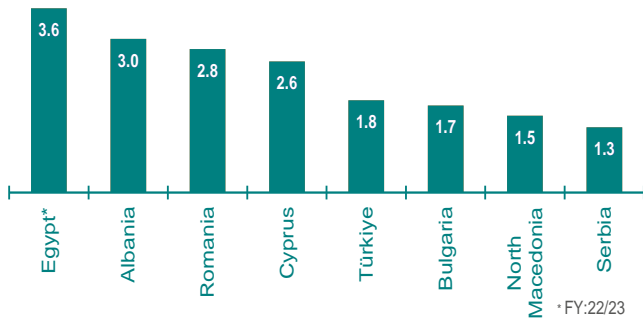
f: NBG forecasts; a: months of imports of GNFS; b: ESA 2010

<b>BULGARIA</b>					
	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023f</b>	<b>2024f</b>
<b>Real Sector</b>					
Nominal GDP (EUR million)	61,638	71,076	84,559	94,682	101,325
GDP per capita (EUR)	8,911	10,393	12,439	14,013	15,085
GDP growth (real, %)	-4.0	7.6	3.4	1.7	2.9
Unemployment rate(ILO definition, %, aop)	6.1	5.3	4.3	4.2	4.1
<b>Prices and Banking</b>					
Inflation (% eop)	0.1	7.8	16.9	5.9	3.2
Inflation (% aop)	1.7	3.3	15.2	10.1	4.0
Loans to the Private Sector (% change, eop)	4.5	8.3	12.2		
Customer Deposits (% change, eop)	10.2	9.0	14.4		
Loans to the Private Sector (% of GDP)	50.7	47.6	44.9		
Retail Loans (% of GDP)	20.8	20.5	19.8		
Corporate Loans (% of GDP)	29.9	27.1	25.1		
Customer Deposits (% of GDP)	73.1	69.1	66.4		
Loans to Private Sector (% of Deposits)	69.4	68.9	67.6		
Foreign Currency Loans (% of Total Loans)	31.1	28.7	25.7		
<b>External Accounts</b>					
Merchandise exports (EUR million)	27,272	34,405	45,926	48,761	50,975
Merchandise imports (EUR million)	29,213	37,291	50,815	53,916	56,398
Trade balance (EUR million)	-1,941	-2,887	-4,889	-5,155	-5,423
Trade balance (% of GDP)	-3.1	-4.1	-5.8	-5.4	-5.4
Current account balance (EUR million)	0,024	-1,316	-0,578	-0,392	-0,130
Current account balance (% of GDP)	0.0	-1.9	-0.7	-0.4	-0.1
Net FDI (EUR million)	2,759	1,303	2,010	2,010	2,160
Net FDI (% of GDP)	4.5	1.8	2.4	2.1	2.1
International reserves (EUR million)	30,848	34,597	38,424	40,792	42,822
International reserves (Months <sup>a</sup> )	11.1	9.8	8.0	8.0	8.0
<b>Public Finance</b>					
Primary balance (% of GDP)	-2.4	-2.4	-0.4	-3.5	-2.5
Fiscal balance (% of GDP)	-2.9	-2.8	-0.8	-4.0	-3.0
Gross public debt <sup>b</sup> (% of GDP)	24.5	23.9	22.9	24.5	26.0
<b>External Debt</b>					
Gross external debt (EUR million)	38,991	41,214	44,431	45,448	46,103
Gross external debt (% of GDP)	63.3	58.0	52.5	48.0	45.5
External debt service (EUR million)	7,041	7,000	8,200	7,100	7,250
External debt service (% of reserves)	22.8	20.2	21.3	17.4	16.9
External debt service (% of exports)	20.4	16.1	14.2	11.5	11.2
<b>Financial Markets</b>					
Base Interest Rate (% eop)	0.0	0.0	1.3	3.3	2.9
Base Interest Rate (% aop)	0.0	0.0	0.2	2.6	3.1
10-Y Bond Yield (% eop)	0.4	0.7	6.0	4.2	3.8
Exchange rate: EUR (eop)	1.956	1.956	1.956	1.956	1.956
Exchange rate: EUR (aop)	1.956	1.956	1.956	1.956	1.956

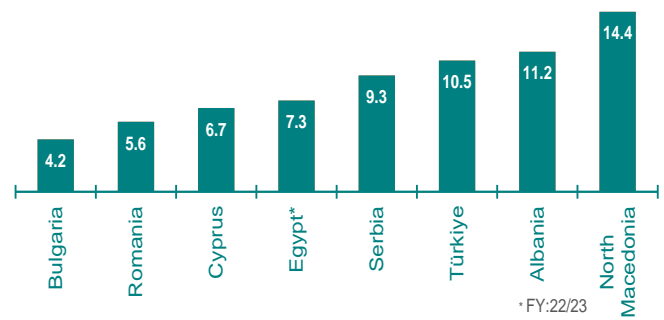
f: NBG forecasts; a: months of imports of GNFS; b: ESA 2010

# REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

Real GDP Growth (% , 2023F)



Unemployment (% , 2023F, aop)



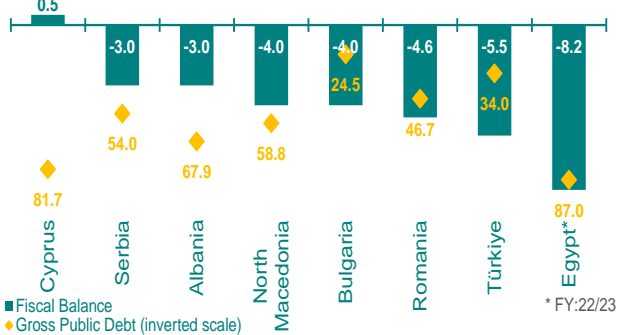
Headline inflation (% , 2023F)



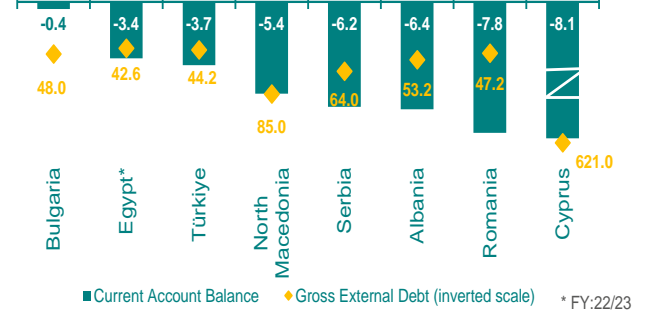
Policy rates (%)



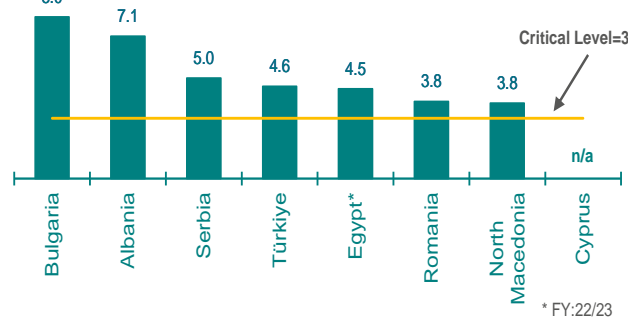
Public Finance (% of GDP, 2023F)



External Accounts (% of GDP, 2023F)



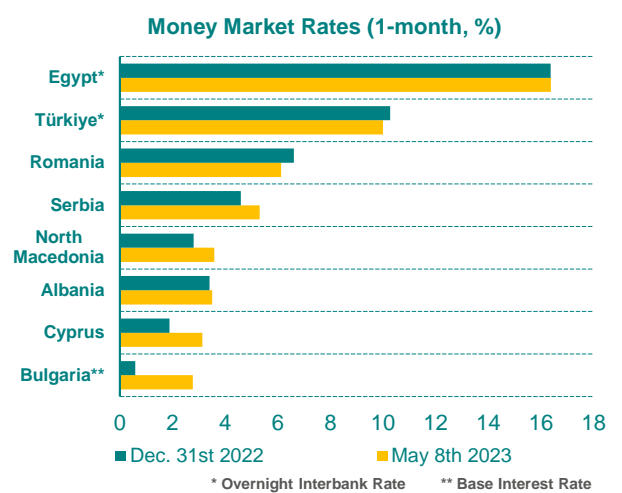
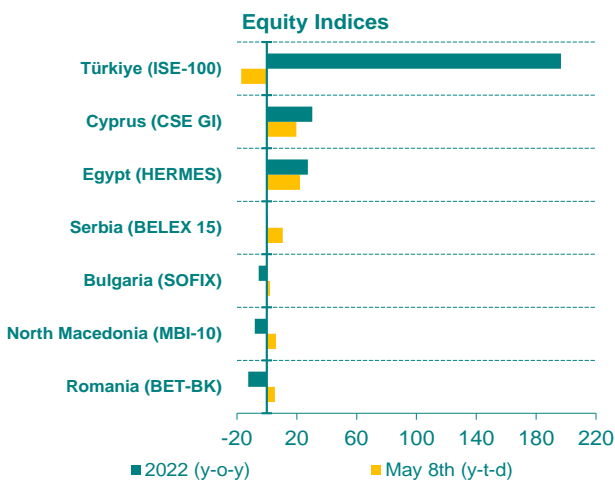
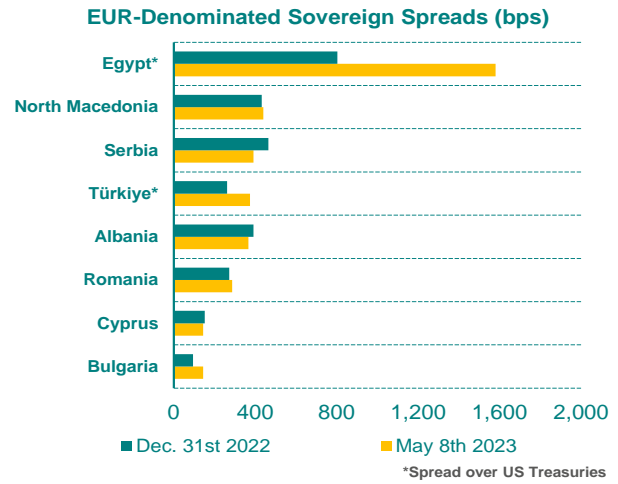
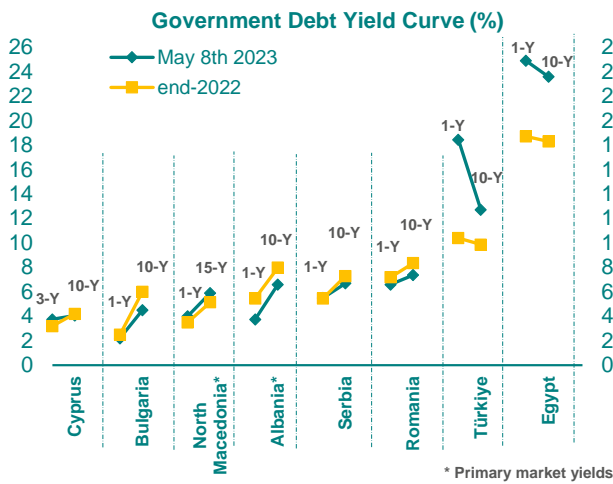
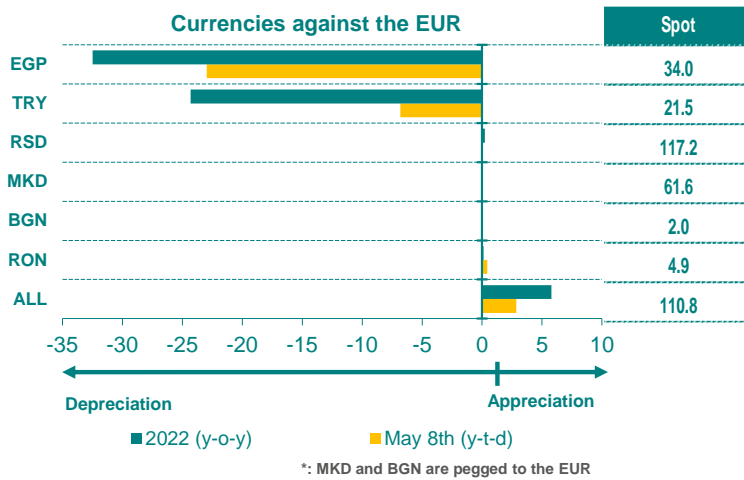
FX Reserves (Months of Imports, 2023F)



Sources: National Sources & NBG estimates



# REGIONAL SNAPSHOT: FINANCIAL MARKETS



Sources: Reuters & NBG estimates

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