NBG - Economic Analysis Division
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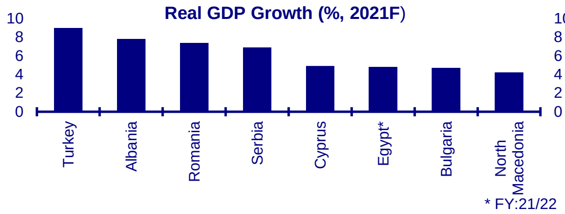
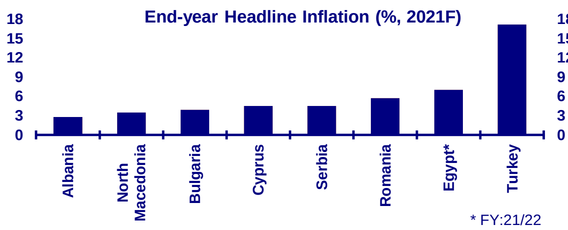
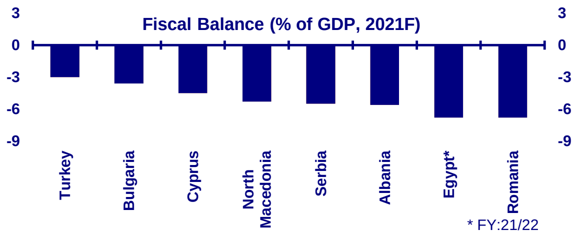
Emerging Markets Analysis

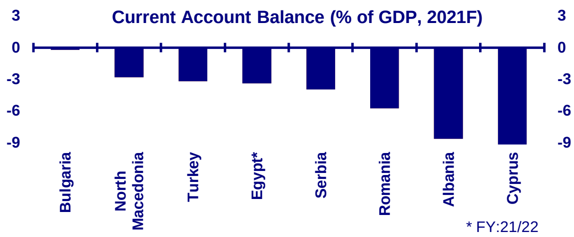
Head: Konstantinos Romanos-Louizos
☎ : +30 210 33 41 225
✉ : romanos.louizos.k@nbg.gr

Louiza Troupi
☎ : +30 210 33 41 696
✉ : troupi.louiza@nbg.gr









Sources: National authorities & NBG estimates

Economic Analysis Division

Emerging Markets Analysis

Bi-Weekly Report

7 - 20 September 2021

GDP growth rebounded in Q2:21 (to 13.0% y-o-y from -0.2% in Q1:21), mainly due to a positive COVID-19-related base effect, lifting the economy above its pre-pandemic size

GDP growth to remain robust in the period ahead, despite ongoing fiscal consolidation

The ongoing political crisis poses a downside risk to the economic outlook

Against the backdrop of economic recovery, the underlying profitability of the banking system improved in H1:21, with ROAE picking up slightly to a robust 7.3%, in line with lower provisioning

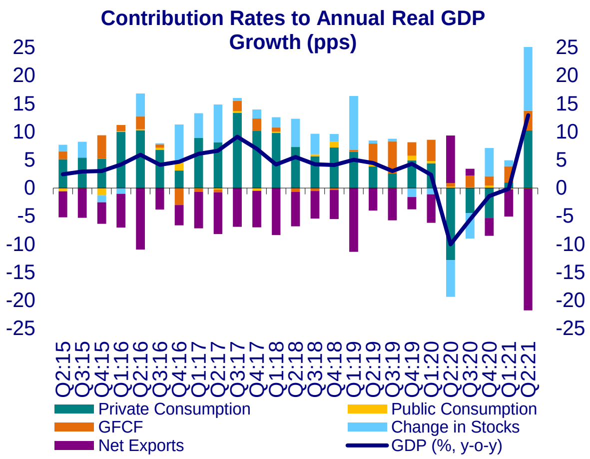
The favourable macroeconomic outlook minimizes the challenges stemming from the expiry of the debt payment moratorium

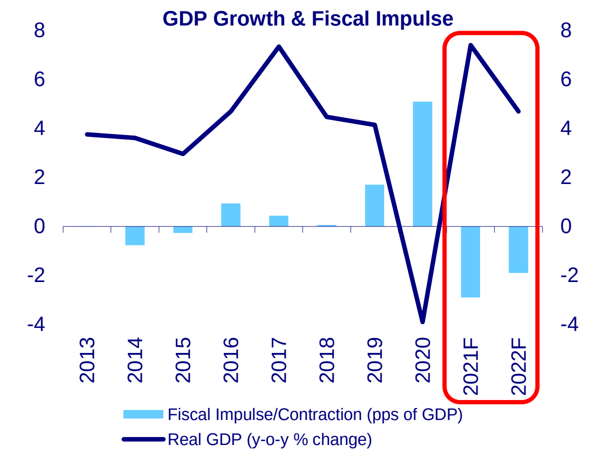
Following a sharp (base effect-driven) rebound in domestic demand, GDP growth surged to 12.8% y-o-y in Q2:21 from -2.0% in Q1:21

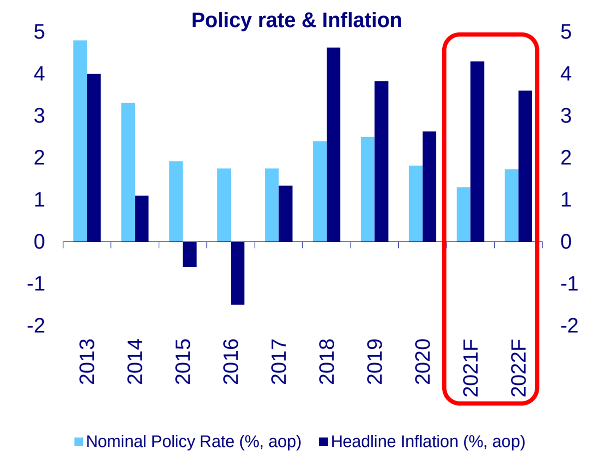
Solid domestic demand and a further recovery in external demand (including for tourism services) should keep GDP growth strong in H2:21

Romania

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







	20 Sep.	3-M F	6-M F	12-M F
1-m ROBOR (%)	1.5	1.7	1.8	2.0
RON/EUR	4.95	4.94	4.94	4.96
Sov. Spread (2024, bps)	73	72	75	80

	20 Sep.	1-W %	YTD %	2-Y %
BET-BK	2,384	-0.9	27.7	34.4

	2018	2019	2020E	2021F	2022F
Real GDP Growth (%)	4.5	4.1	-3.9	7.4	4.1
Inflation (eop, %)	3.3	4.0	2.1	5.7	3.2
Cur. Acct. Bal. (% GDP)	-4.6	-4.9	-5.2	-5.8	-5.3
Fiscal Bal. (% GDP)	-2.9	-4.6	-9.7	-6.8	-5.0

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

GDP growth rebounded in Q2:21 (to 13.0% y-o-y from -0.2% in Q1:21), mainly due to a positive COVID-19-related base effect, lifting the economy above its pre-pandemic size. Easing restrictions and improving confidence, in the wake of the launch of a COVID-19 vaccination campaign, led to a massive rebound in domestic demand in Q2:21, given the sizeable positive base effect from the plunge in economic activity at the onset of the pandemic in Q2:20. Private consumption and the rebuilding of stocks emerged as the main growth drivers in Q2:21 (see chart). Unsurprisingly, net exports deteriorated sharply at the same time, in line with stronger domestic demand. Note that, on a sequential basis, GDP growth moderated further to 1.8% q-o-q s.a. from 2.5% in Q1:21 and 4.4% on average in Q3-Q4:20, suggesting that economic momentum has already peaked.

GDP growth to remain robust in the period ahead, despite ongoing fiscal consolidation. Romania is currently facing a new COVID-19 wave, which is due to peak over the next few weeks. Still, strict lockdown measures are unlikely to be reinstated, as hospitalizations and deaths are expected to be lower than before, due to increasing vaccination coverage (which is yet among the lowest in the EU).

In this environment, we expect economic activity to remain strong, with its growth pace moderating, however, mainly due to fading COVID-19 base effects. Private consumption is set to remain the main growth driver, supported by a still strong labour market. Fixed investment should also gain momentum, driven by higher EU-backed capital spending. Note that Romania is eligible to receive funds worth c. 35.0% of FY:19 GDP under the NGEU and the MFF schemes in 2021-27, with the historical low EU funds absorption rate posing, however, challenges in this regard. Despite the recovery in the EU, Romania's main trade partner (absorbing 75% of its exports), net exports will remain a drag on overall growth, as reviving domestic demand feeds into imports (the latter account for 112% of GDP as compared with 62% for exports).

On the downside, the previous year's fiscal stimulus would continue to be withdrawn at a fast pace in H2:21. This trend is set to continue next year as well, albeit at a relatively slower pace, with the budget deficit projected to fall under the EU threshold of 3% of GDP only after 2024, reflecting a weak starting point, due to pre-pandemic excesses.

At the same time, monetary conditions are set to remain accommodative, helping to cushion the impact of fiscal consolidation on GDP growth. Note that, against an increasingly challenging backdrop, reflecting widening external imbalances, on the one hand, and the upward shift in the inflation outlook, on the other hand, the NBR stands ready to deliver a 25 bp rate hike as early as in Q4:21, especially in view of the shrinking interest rate differential between Romania and its peers. Another 25 bp hike is expected in early 2022, with *ex-post* real rates, however, due to remain in deep negative territory over the projection horizon.

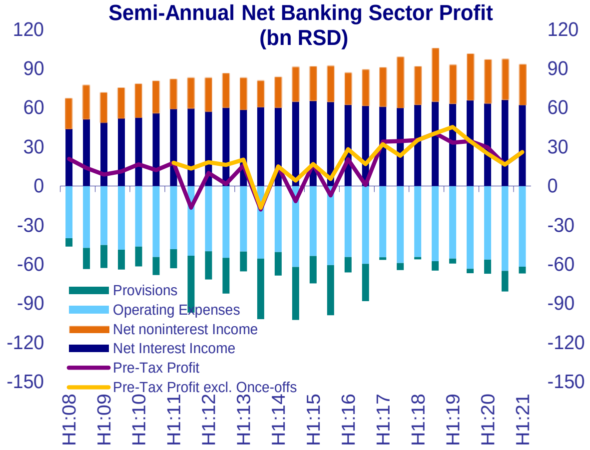
All said, we see FY:21 GDP growth to 7.4%, among the highest in the EU. For FY:22, we project GDP growth to normalise to 4.7%, still above its long-term potential rate (of c. 3.0%), with domestic demand partially rebalancing towards investment.

The ongoing political crisis poses a downside risk to the economic outlook. The crisis was triggered by the withdrawal of the liberal USR+ alliance from the ruling coalition, led by the centre-right PNL and also comprising the Hungarian minority party, UDMR, following the dismissal of one of its ministers over a dispute on policy priorities under Romania's Recovery & Resilience Plan (RRP). It still remains to be seen whether the PNL will manage to form a minority Government or snap elections will be called. In any case, should delays in the implementation of the RRP emerge, GDP growth could be significantly affected. Similarly, any disruption in fiscal consolidation could undermine investors' confidence.

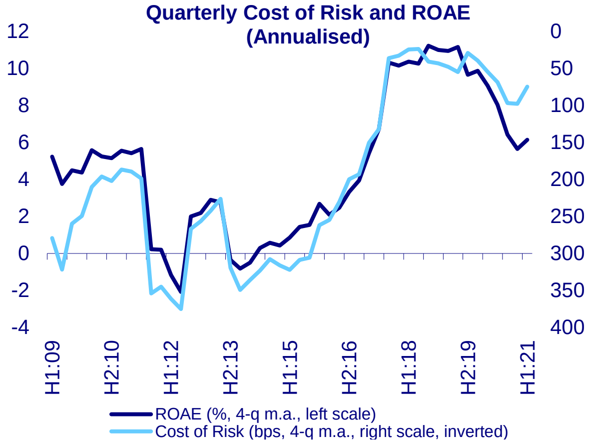
Serbia

BB+ / Ba2 / BB+ (S&P / Moody's / Fitch)

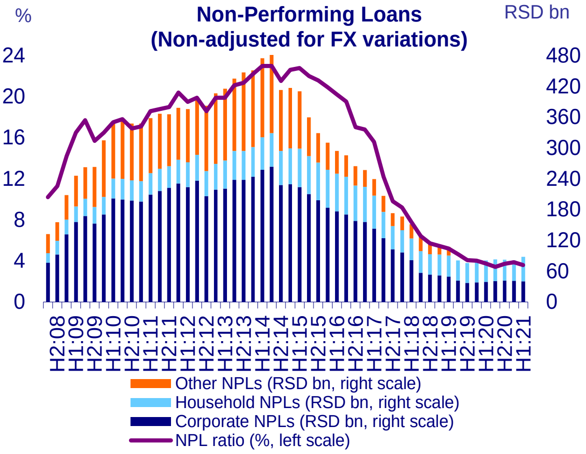
Semi-Annual Net Banking Sector Profit (bn RSD)



Quarterly Cost of Risk and ROAE (Annualised)



Non-Performing Loans (Non-adjusted for FX variations)



	20 Sep.	3-M F	6-M F	12-M F
1-m BELIBOR (%)	0.6	0.7	0.8	1.0
RSD/EUR	117.5	117.5	117.5	117.5
Sov. Spread (2029, bps)	194	190	180	170

	20 Sep.	1-W %	YTD %	2-Y %
BELEX-15	797	-1.3	6.5	5.5

	2018	2019	2020	2021F	2022F
Real GDP Growth (%)	4.5	4.2	-1.0	6.9	4.4
Inflation (eop, %)	2.0	1.9	1.3	4.5	2.5
Cur. Acct. Bal. (% GDP)	-4.8	-6.9	-4.3	-4.0	-3.9
Fiscal Bal. (% GDP)	0.6	-0.2	-8.1	-5.5	-3.5

Sources: Reuters, NBS & NBG estimates

Against the backdrop of solid economic recovery, the underlying profitability of the banking system improved in H1:21, with ROAE picking up slightly to a robust 7.3%, in line with lower provisioning. Adjusted for one-offs (namely an exceptional high gain of RSD 4.6bn made by AIK Bank in H1:20, through its subsidiary in Slovenia), the domestic banking sector's pre-tax profits are estimated to have increased by 4.5% y-o-y to RSD 26.1bn (c. 0.4% of GDP) in H1:21. As a result, (annualised) ROAE and ROAA rose to 7.3% and 1.1%, respectively, in H1:21 from an estimated 7.1% and 1.2% in H1:20 (with corresponding FY:20 figures standing at 5.8% and 1.0%).

Following the front-loading of loan loss provisioning at the onset of the pandemic, the cost of risk (CoR) dropped sharply in H1:21. With the economy having more than recouped its COVID-19-induced losses (by c. 3.0%), the CoR fell by 47 bps y-o-y to 38 bps (annualised) in H1:21, well below the (4-year high) FY:20 outcome of 102 bps. Note that the NPL ratio continued to subside, hitting a record low of 3.6% in Q2:21 -- below its pre-crisis level -- with the bulk of the improvement, due, however, to the impact of the forbearance measures enacted (debt repayment moratorium, effective until mid-year) and fast credit expansion.

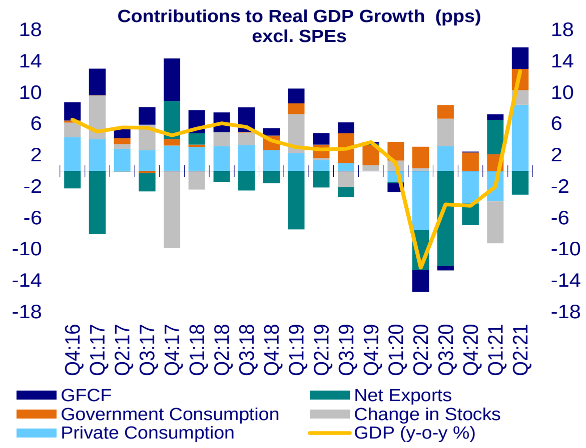
Despite resilient top line revenue, pre-provision income came under pressure in H1:21, on exceptionally high operating expenses. Regarding income sources, net non-interest income (NNII, excluding non-recurrent revenues) emerged as the sole growth driver in H1:21 (up 7.6% y-o-y), reflecting higher net fees and commission income, following the strong rebound in economic activity. Stronger NNII more than compensated for the (modest) deterioration in net interest income (NII, down 1.9% y-o-y). The latter came on the back of: i) negative base effects from the enactment of the debt moratorium in mid-March 2020; ii) a faster pace of deposit growth than loan growth (up 11.6% y-o-y in H1:21 versus 8.3% y-o-y); and iii) a further compression in the net interest margin (NIM), amid accommodative monetary policy conditions.

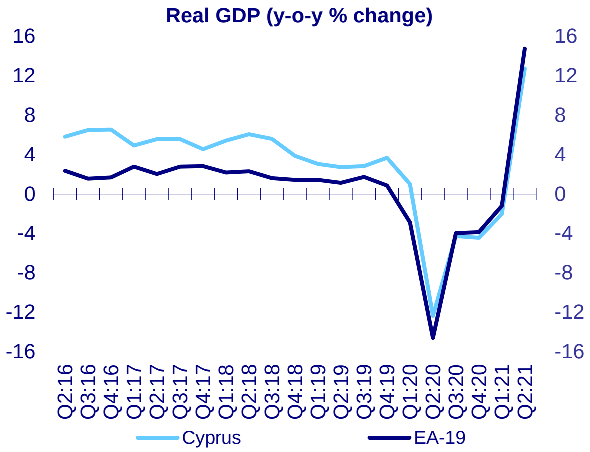
The slight improvement in top line revenue (up 1.1% y-o-y in H1:21) was more than offset, however, by the jump in operating expenses (up 9.7% y-o-y). Indeed, despite strict personnel spending, operating expenses surged, reflecting increased IT investments and, probably, some once-off expenses related to M&As. As a result, banking sector efficiency deteriorated, with the cost-to-income ratio increasing by 5.2 pps y-o-y to 66.4% in H1:21 from 62.6% in FY:20.

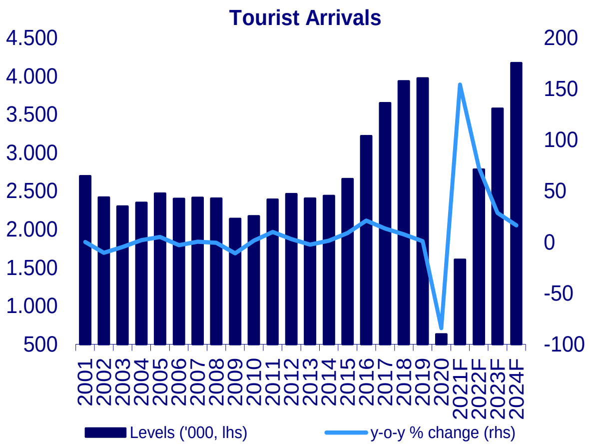
The favourable macroeconomic outlook minimizes the challenges stemming from the expiry of the debt payment moratorium. Bottom line is expected to strengthen further in H2:21, mainly driven by solid expansion in NNII and a rebound in NII. The latter should be underpinned by strong credit expansion and the resumption of debt repayments, following the expiry of forbearance measures. At the same time, we expect loan loss provisioning to remain relatively subdued, reflecting limited payment arrears, amid strong economic growth (see table). All said, we expect ROAE to pick-up to 6.8% in FY:21 from 5.8% in FY:20 (or 6.5% unadjusted for the aforementioned once-offs). Note that the increasing number of lawsuits contesting the legality of loan processing fees banks are facing could pose additional costs to their profitability. Importantly, the banking system remains well-capitalised (the total capital adequacy ratio stands at 22.3%, well above the regulatory floor of 8.0%), suggesting that there is significant headroom to absorb any potential stress.

Cyprus

BBB- / Ba1 / BBB- (S&P / Moody's / Fitch)







	20 Sep.	3-M F	6-M F	12-M F
1-m EURIBOR (%)	-0.56	-0.56	-0.55	-0.53
EUR/USD	1.17	1.18	1.19	1.20
Sov. Spread (2025. bps)	43	45	50	60

	20 Sep.	1-W %	YTD %	2-Y %
CSE Index	67	-1.1	17.9	-1.1

	2018	2019	2020	2021F	2022F
Real GDP Growth (%)	5.2	3.1	-5.1	4.9	4.2
Inflation (eop. %)	1.7	0.7	-1.1	4.5	1.8
Cur. Acct. Bal. (% GDP)	-3.9	-6.3	-11.9	-9.3	-6.5
Fiscal Bal. (% GDP)	-3.5	1.5	-5.7	-4.5	-3.0

Sources: Reuters, CYSTAT & NBG estimates

Following a sharp (base effect-driven) rebound in domestic demand, GDP growth surged to 12.8% y-o-y in Q2:21 from -2.0% in Q1:21. As expected, private consumption emerged as the main engine of economic expansion in Q2:21 (see chart), reflecting looser COVID-19 restrictions and a sharp improvement in consumer confidence, on the back of the fast vaccine rollout (with the share of people fully vaccinated standing at 59.5% in early-September, in line with the EU average). Investment also picked-up in Q2:21, driven by stronger residential construction activity, following, *inter alia*, the launch of a state-subsidised mortgage rate scheme (effective by year-end). Unsurprisingly, net exports' (excluding SPEs) contribution to overall growth turned negative in Q2:21, as stronger domestic demand fed into imports. The drag from net exports would have been larger had exports of non-tourism services -- mainly financial, transport (shipping) and business related (especially ICT) services -- not strengthened, reflecting Cyprus' growing export diversification. Exports of tourism services also rebounded strongly in Q2:21 (with tourist arrivals reaching 0.3mn in Q2:21 against almost nil in Q2:20 -- yet standing at just 25% of their Q2:19 level).

It should be noted that economic growth lost momentum in Q2:21, with GDP growing by a mere 0.2% q-o-q s.a. against a rise of 1.7% in Q1:21. This slowdown was attributed to the impact of the severe 3rd COVID-19 wave and previous quarters' economic overperformance. Indeed, at current levels, the size of the Cypriot economy accounts for 97.4% of its pre-COVID-19 size, a performance in line with the euro area average.

Solid domestic demand and a further recovery in external demand (including for tourism services) should keep GDP growth strong in H2:21. Despite the re-imposition of some social-distancing measures in Q3:21, due to the rapid spread of an infectious COVID-19 variant, and the restart of debt repayments, following the expiry of a loan repayment moratorium in mid-year, we expect private consumption to grow at a solid pace in H2:21, reflecting: i) a further improvement in sentiment, underpinned by both high vaccination rates and intensive testing; ii) the release of strong pent-up demand (note that retail deposits have increased by 17.3 pps of GDP since end-2019, to 124% of GDP in July); and iii) substantial positive spill-overs from the envisaged rebound in tourism (see below) and related sectors.

Fixed investment should also maintain steam in H2:21, driven by public capital spending. At the same time, private investment will continue to benefit from accommodative financing conditions (which are supplemented by state loan guarantees and a subsidised interest rate scheme) and improving investment sentiment. Note, however, that the abolition of the "Golden Visa" scheme bodes ill for high-end residential construction activity.

Importantly, net exports' contribution to overall growth is set to improve in H2:21, reflecting: i) strong financial, shipping and business exports; and ii) the recovery in tourist inflows. The latter are set to increase by more than three times their level in H2:20 in the remainder of the year, supported by the fast vaccination rollout in Cyprus' main source markets. Overall, we see tourist arrivals growing by 150% in FY:21 to just 40% of their pre-COVID-19 level, with full recovery not expected before 2024.

All said, we see GDP growth reaching to 4.9% in FY:21, almost fully recouping its COVID-19-induced losses. Amid further fiscal consolidation, we expect GDP growth to moderate slightly to 4.2% in FY:22, still above its long-term potential (of c. 2.5%), with net exports providing a small positive contribution to overall growth and domestic demand rebalancing towards EU-funded investment. Note that Cyprus is due to receive EUR 1.2bn in 2021-26 (5.4% of the 2021 GDP) from EU's Recovery & Resilience Fund, with the country's strong track record boding well for a fast and full absorption of the available funds.

ROMANIA	2018	2019	2020	2021f	2022f
Real Sector					
Nominal GDP (EUR million)	204,633	223,104	218,306	240,777	259,468
GDP per capita (EUR)	10,477	11,497	11,251	12,410	13,374
GDP growth (real, %)	4.5	4.1	-3.9	7.4	4.7
Unemployment rate(ILO definition, %, aop)	4.2	3.9	5.0	5.4	5.0
Prices and Banking					
Inflation (%, eop)	3.3	4.0	2.1	5.7	3.2
Inflation (%, aop)	4.6	3.8	2.6	4.4	3.7
Loans to the Private Sector (% change, eop)	7.9	8.4	8.4		
Customer Deposits (% change, eop)	9.2	10.2	10.2		
Loans to the Private Sector (% of GDP)	25.6	25.9	25.9		
Retail Loans (% of GDP)	14.0	14.1	14.1		
Corporate Loans (% of GDP)	11.6	11.8	11.8		
Customer Deposits (% of GDP)	32.7	33.0	33.0		
Loans to Private Sector (% of Deposits)	78.4	78.4	78.4		
Foreign Currency Loans (% of Total Loans)	33.7	34.4	34.4		
External Accounts					
Merchandise exports (EUR million)	61,820	63,062	57,551	66,342	70,333
Merchandise imports (EUR million)	77,160	80,918	76,717	86,975	91,832
Trade balance (EUR million)	-15,340	-17,856	-19,166	-20,632	-21,499
Trade balance (% of GDP)	-7.5	-8.0	-8.8	-8.6	-8.3
Current account balance (EUR million)	-9,495	-10,913	-11,421	-13,868	-13,704
Current account balance (% of GDP)	-4.6	-4.9	-5.2	-5.8	-5.3
Net FDI (EUR million)	4,944	4,848	1,856	2,784	3,480
Net FDI (% of GDP)	2.4	2.2	0.9	1.2	1.3
International reserves (EUR million)	33,065	32,926	38,527	40,743	41,469
International reserves (Months[a])	4.3	4.0	5.1	4.7	4.5
Public Finance					
Primary balance (% of GDP)	-1.5	-3.4	-8.3	-5.3	-3.5
Fiscal balance (% of GDP)	-2.9	-4.6	-9.7	-6.8	-5.0
Gross public debt [b] (% of GDP)	34.6	35.0	47.0	49.8	51.3
External Debt					
Gross external debt (EUR million)	99,841	109,783	125,927	133,391	140,891
Gross external debt (% of GDP)	48.8	49.2	57.7	55.4	54.3
External debt service (EUR million)	19,132	17,442	16,372	16,600	17,200
External debt service (% of reserves)	57.9	53.0	42.5	40.7	41.5
External debt service (% of exports)	22.3	19.4	20.1	17.9	17.5
Financial Markets					
Policy rate (1-w repo rate, %, eop)	2.5	2.5	1.5	1.5	1.8
Policy rate (1-w repo rate, %, aop)	2.4	2.5	1.8	1.3	1.7
10-Y Bond Yield (%, eop)	4.8	4.5	3.1	3.8	4.0
Exchange rate: EUR (eop)	4,652	4,786	4,863	4,935	4,970
Exchange rate: EUR (aop)	4,651	4,743	4,835	4,915	4,953

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

SERBIA	2018	2019	2020	2021f	2022f
Real Sector					
Nominal GDP (EUR million)	42,939	46,017	46,493	51,438	55,536
GDP per capita (EUR)	6,149	6,626	6,739	7,446	8,071
GDP growth (real, %)	4.5	4.2	-1.0	6.9	4.4
Unemployment rate (%, aop)	13.7	11.2	9.7	11.6	10.0
Prices and Banking					
Inflation (%, eop)	2.0	1.9	1.3	4.5	2.5
Inflation (%, aop)	2.0	1.9	1.6	3.3	3.4
Loans to the Private Sector (% change, eop)	9.9	8.9	12.2		
Customer Deposits (% change, eop)	14.9	7.8	17.4		
Loans to the Private Sector (% of GDP)	43.5	44.4	49.4		
Retail Loans (% of GDP)	20.1	20.5	22.8		
Corporate Loans (% of GDP)	23.4	23.8	26.6		
Customer Deposits (% of GDP)	44.9	45.3	52.7		
Loans to Private Sector (% of Deposits)	96.9	98.0	93.6		
Foreign Currency Loans (% of Total Loans)	67.0	66.9	62.7		
External Accounts					
Merchandise exports (EUR million)	15,106	16,415	16,032	17,349	18,312
Merchandise imports (EUR million)	20,191	22,038	21,257	22,978	24,244
Trade balance (EUR million)	-5,085	-5,623	-5,224	-5,629	-5,932
Trade balance (% of GDP)	-11.8	-12.2	-11.2	-10.9	-10.7
Current account balance (EUR million)	-2,076	-3,161	-1,981	-2,049	-2,172
Current account balance (% of GDP)	-4.8	-6.9	-4.3	-4.0	-3.9
Net FDI (EUR million)	3,157	3,551	2,902	3,338	3,671
Net FDI (% of GDP)	7.4	7.7	6.2	6.5	6.6
International reserves (EUR million)	11,262	13,379	13,492	16,390	17,739
International reserves (Months[a])	5.4	5.7	6.1	6.9	7.1
Public Finance					
Primary balance (% of GDP)	2.8	1.8	-6.1	-3.7	-1.7
Fiscal balance (% of GDP)	0.6	-0.2	-8.1	-5.5	-3.5
Central Government debt (% of GDP)	54.4	52.9	58.2	59.0	58.3
External Debt					
Gross external debt (EUR million)	26,662	28,254	30,813	33,434	35,099
Gross external debt (% of GDP)	62.1	61.4	66.3	65.0	63.2
External debt service (EUR million)	5,600	6,400	3,900	4,800	4,900
External debt service (% of reserves)	49.7	47.8	28.9	29.9	28.2
External debt service (% of exports)	26.4	27.4	17.6	19.8	19.2
Financial Markets					
Policy rate (2-w repo rate, %, eop)	3.0	2.3	1.0	1.0	1.3
Policy rate (2-w repo rate, %, aop)	3.1	2.7	1.5	1.0	1.1
5-Y T-bill rate [b] (%, eop)	n.a.	n.a.	2.6	2.2	2.5
Exchange rate: EUR (eop)	118.2	117.5	117.5	117.5	117.5
Exchange rate: EUR (aop)	118.1	117.7	117.5	117.5	117.5

f: NBG forecasts; a: months of imports of GNFS; b: primary market

CYPRUS	2018	2019	2020	2021f	2022f
Real Sector					
Nominal GDP (EUR million)	21,432	22,287	20,841	22,408	24,027
GDP per capita (EUR)	24.806	25.442	23.522	25.009	26.520
GDP growth (real, %)	5.2	3.1	-5.1	4.9	4.2
Unemployment rate (%, aop)	8.4	7.1	7.6	7.7	7.1
Prices and Banking					
Inflation (%, eop)	1.7	0.7	-1.1	4.5	1.8
Inflation (%, aop)	1.4	0.3	-0.6	2.5	2.9
Loans to the Private Sector (% change, eop)	-22.0	-7.4	-5.6		
Customer Deposits (% change, eop)	-1.9	0.0	-0.6		
Loans to the Private Sector (% of GDP)	154.3	137.4	138.7		
Retail Loans (% of GDP)	69.5	63.3	64.3		
Corporate Loans (% of GDP)	84.9	74.1	74.4		
Customer Deposits (% of GDP)	193.3	185.9	197.5		
Loans to Private Sector (% of Deposits)	79.8	73.9	70.2		
Foreign Currency Loans (% of Total Loans)	- - -	- - -	- - -		
External Accounts					
Merchandise exports (EUR million)	3,689	3,106	2,964	3,077	3,187
Merchandise imports (EUR million)	8,225	7,741	7,141	7,498	7,783
Trade balance (EUR million)	-4,537	-4,634	-4,177	-4,422	-4,596
Trade balance (% of GDP)	-21.2	-20.8	-20.0	-19.7	-19.1
Current account balance (EUR million)	-0,842	-1,406	-2,476	-2,093	-1,554
Current account balance (% of GDP)	-3.9	-6.3	-11.9	-9.3	-6.5
Net FDI (EUR million)	4,734	5,312	2,020	2,424	3,151
Net FDI (% of GDP)	22.1	23.8	9.7	10.8	13.1
International reserves (EUR million)	- - -	- - -	- - -	- - -	- - -
International reserves (Months[a])	- - -	- - -	- - -	- - -	- - -
Public Finance					
Primary balance [b] (% of GDP)	-1.2	3.8	-3.6	-2.5	-1.0
Fiscal balance [b] (% of GDP)	-3.5	1.5	-5.7	-4.5	-3.0
Gross public debt (% of GDP)	99.2	94.0	118.2	111.5	105.2
External Debt					
Gross external debt (EUR million)	192,933	189,212	189,307	190,000	188,500
Gross external debt (% of GDP)	900.2	849.0	908.4	847.9	784.5
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	0,0	0,0	0,0	0,0
Policy rate (ECB refinancing rate, %, aop)	0,0	0,0	0,0	0,0	0,0
3-Y T-bill rate (%, eop)	0,8	-0,1	-0,1	-0,1	0,2
Exchange rate: USD (eop)	1,147	1,121	1,221	1,180	1,210
Exchange rate: USD (aop)	1,181	1,119	1,142	1,193	1,195

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