OXYGEN EVENTS CONFERENCE

GALA PERFORMANCE 2017

MONETARY AND FISCAL POLICIES DURING THE NEXT RECESSION

- THE CASE OF ROMANIA -

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BUCHAREST

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MOTTO(S)

“There have been three great inventions since the beginning of time: fire, the wheel, and central banking.”

Will Rogers

“Victorians heard with grave attention that the Bank Rate had been raised. They did not know what it meant. But they knew that it was an act of extreme wisdom.”

John Kenneth Galbraith

"3.0 percent means 3.0 percent and not 3.2 percent.“

Theo Waigel

"The four most dangerous words in finance are 'this time is different'.”

Martin Wolf

CONTENT

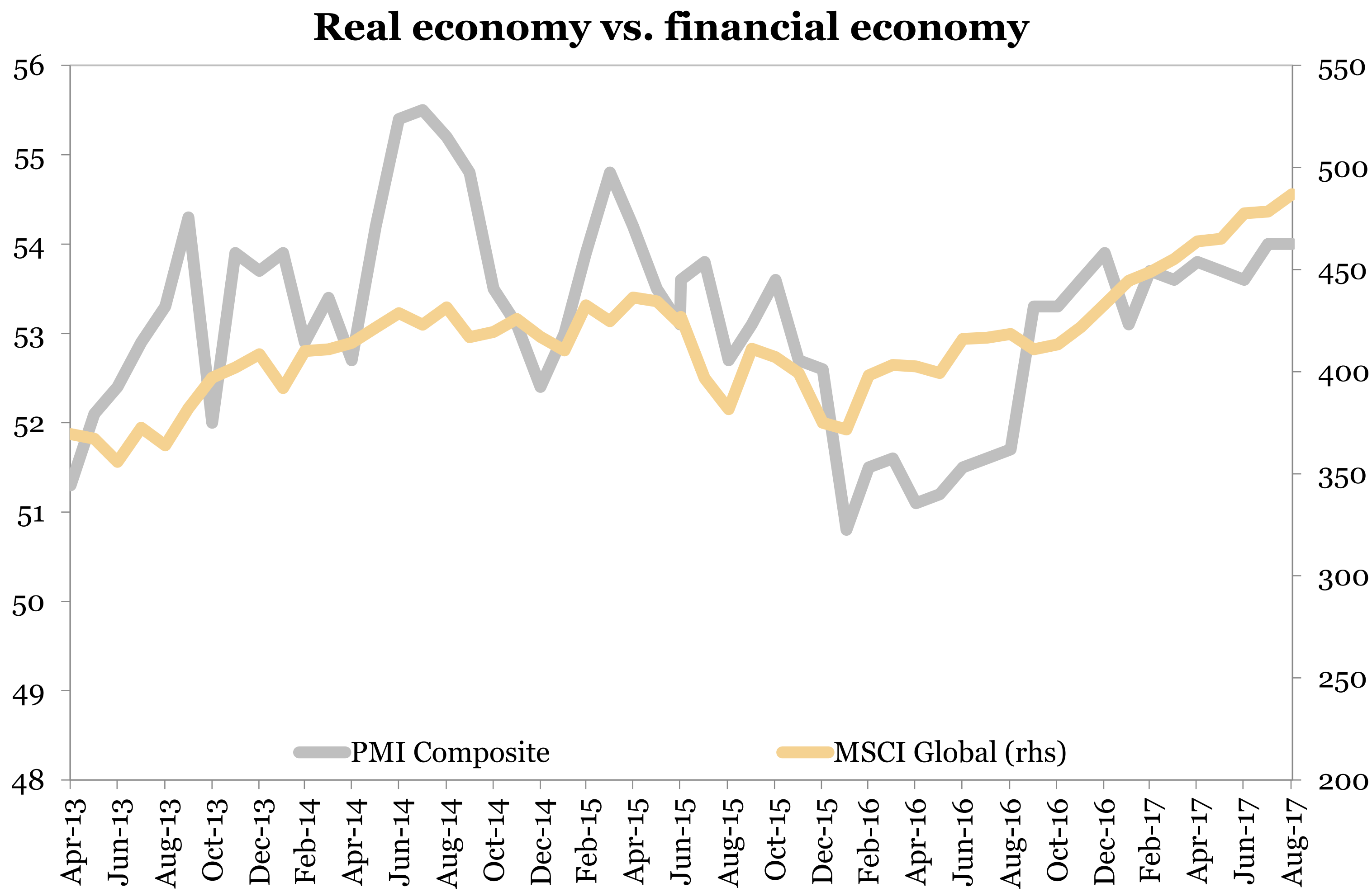
INTRODUCTION

END-OF-CYCLE POLICY-MIX CHALLENGES

- The accumulation of maturity signs for the global post-crisis cycle
- Romanian economy highly integrated with the EU economic cycle
- Strong divergence between the overheating consumption and sluggish investments
- The acceleration of the economy accompanied by the return of twin deficits
- An expansionary and pro-cyclical, but unsustainable policy-mix
- At present there lacks maneuver room in case of shocks
- A rebalance of the policy-mix starting 2018 very likely
- Several challenges in terms of real economic convergence and development

GLOBAL AND EUROPEAN MACROECONOMIC CLIMATE

STRONG GLOBAL MACRO-FINANCIAL CLIMATE

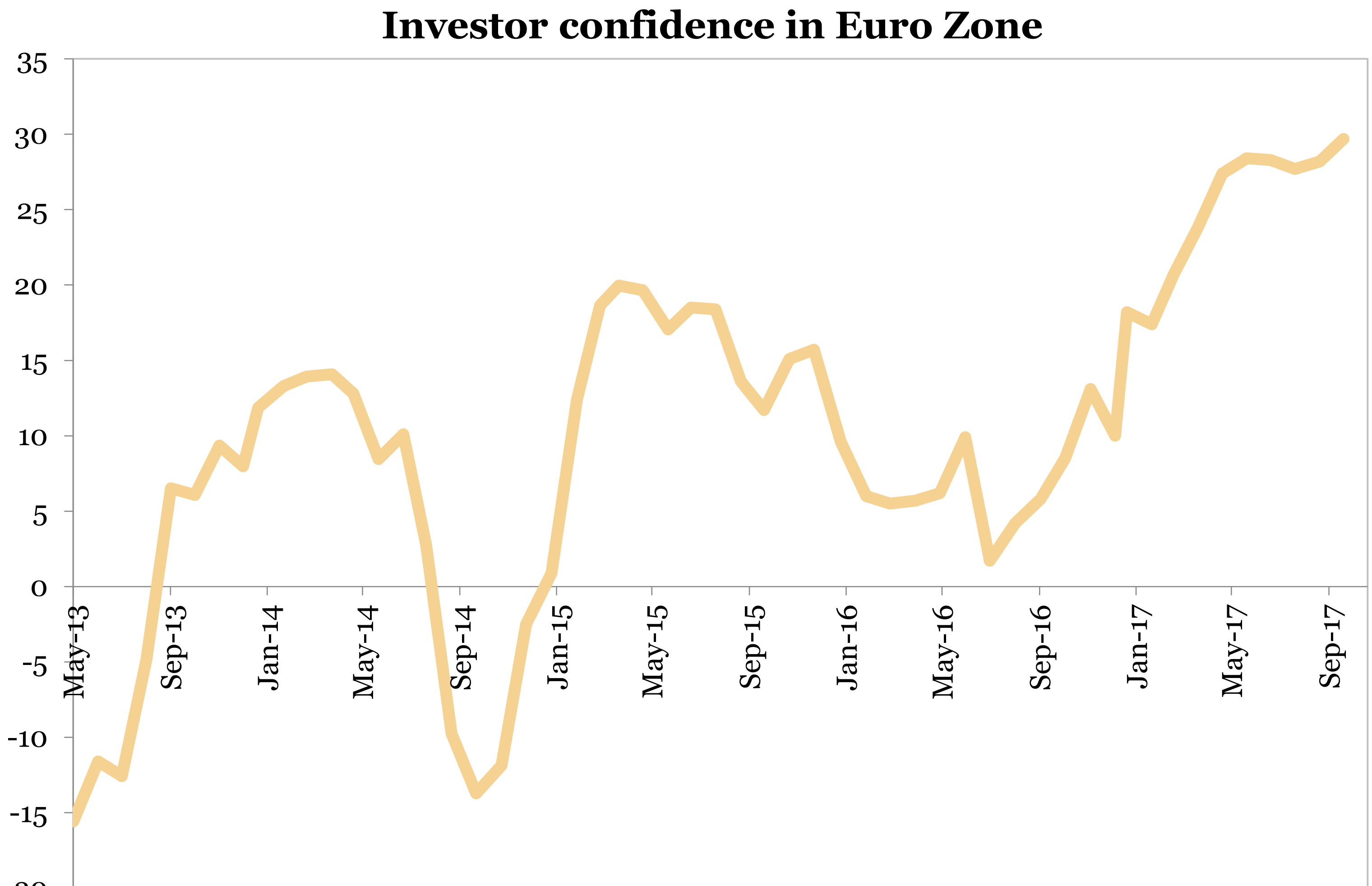


Source: Bloomberg

US ECONOMY – THE MATURITY OF THE CYCLE

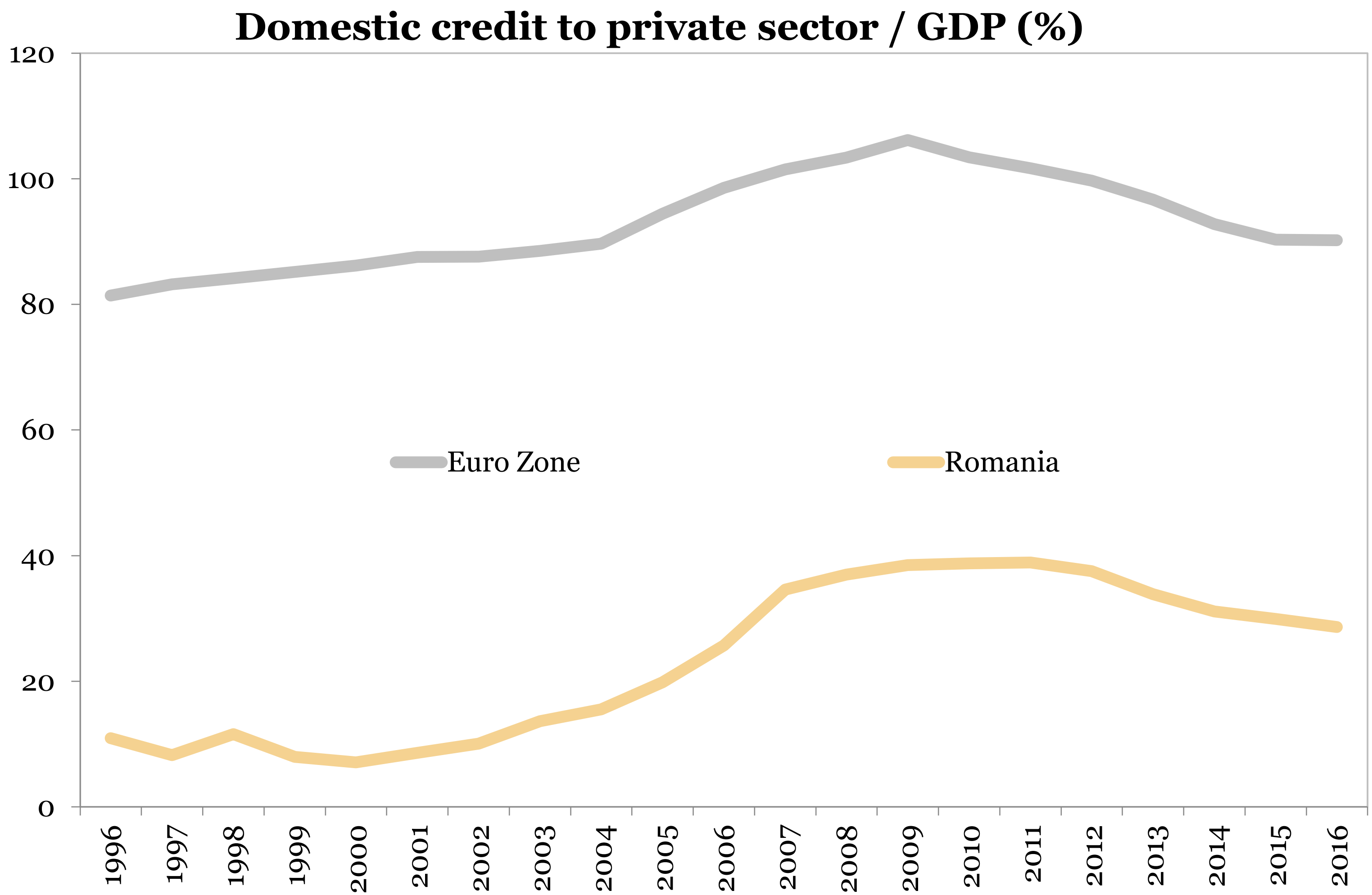
Source: BT based on US Bureau of Labor Statistics (BLS)

EU ECONOMY – AT THE PEAK OF THE CYCLE



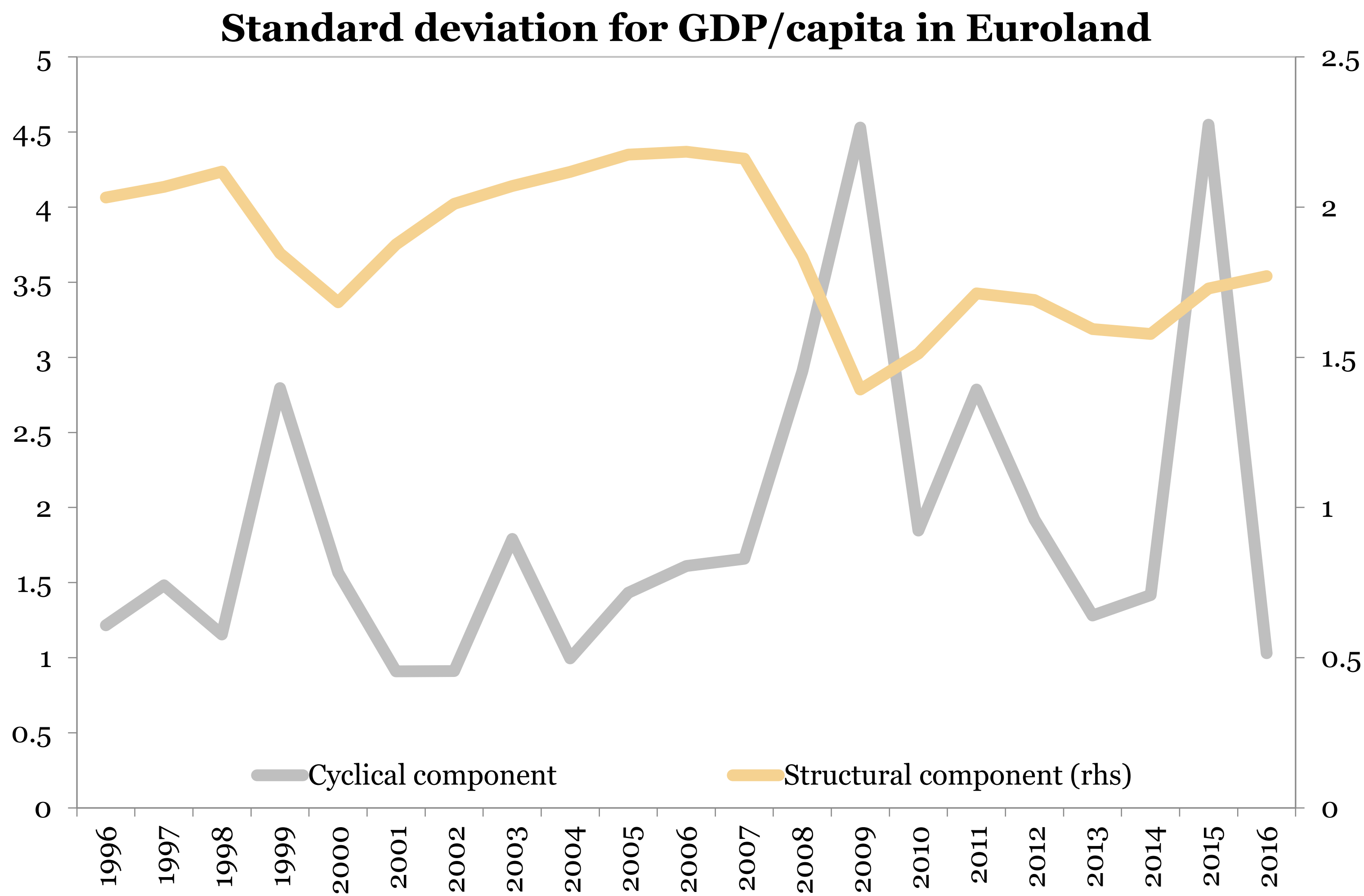
Source: Sentix

THE END OF DELEVERAGING IN EUROPE



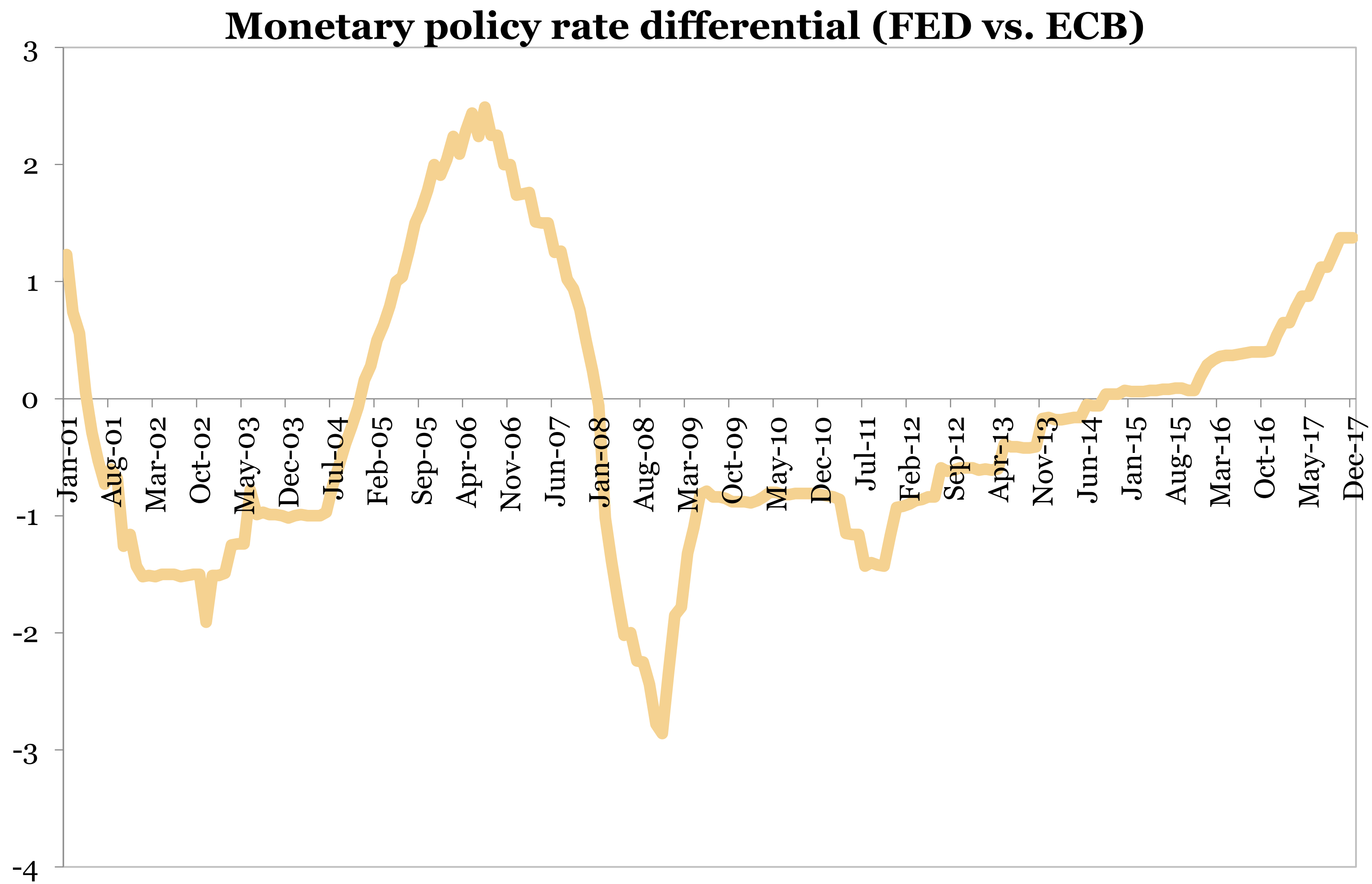
Source: Eurostat, NBR, BT

INCREASING CONVERGENCE IN EUROLAND



Source: own estimates based on the methodology, using Eurostat, AMECO databases

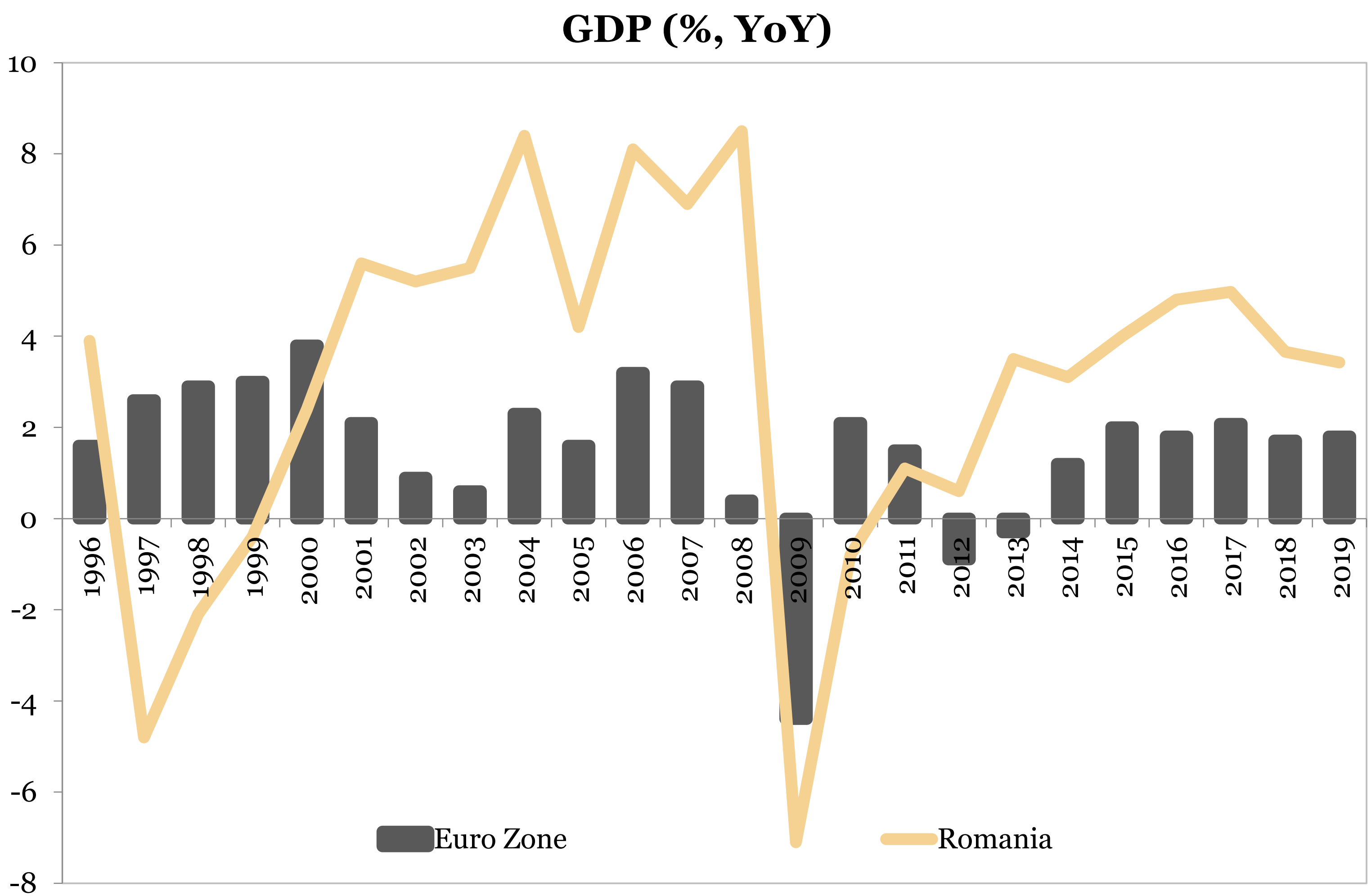
UNSUSTAINABLE MONETARY DIVERGENCE



Source: Federal Reserve, European Central Bank, BT forecasts

ROMANIAN ECONOMY IN THE POST-CRISIS CYCLE

ROMANIA – THE CHAMPION OF GROWTH IN EU

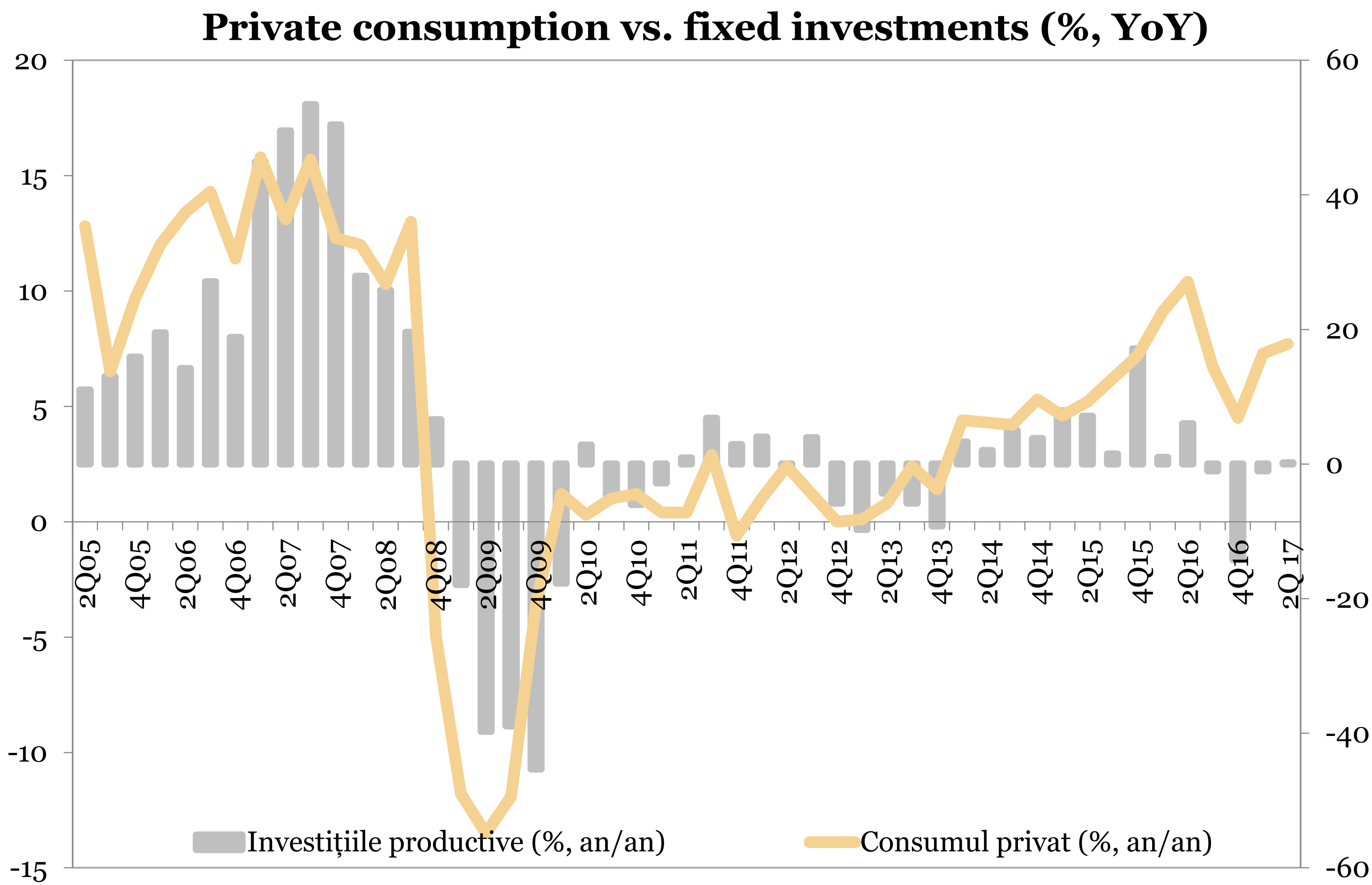


Source: Eurostat, BT forecasts

THE PEAK OF THE CYCLE

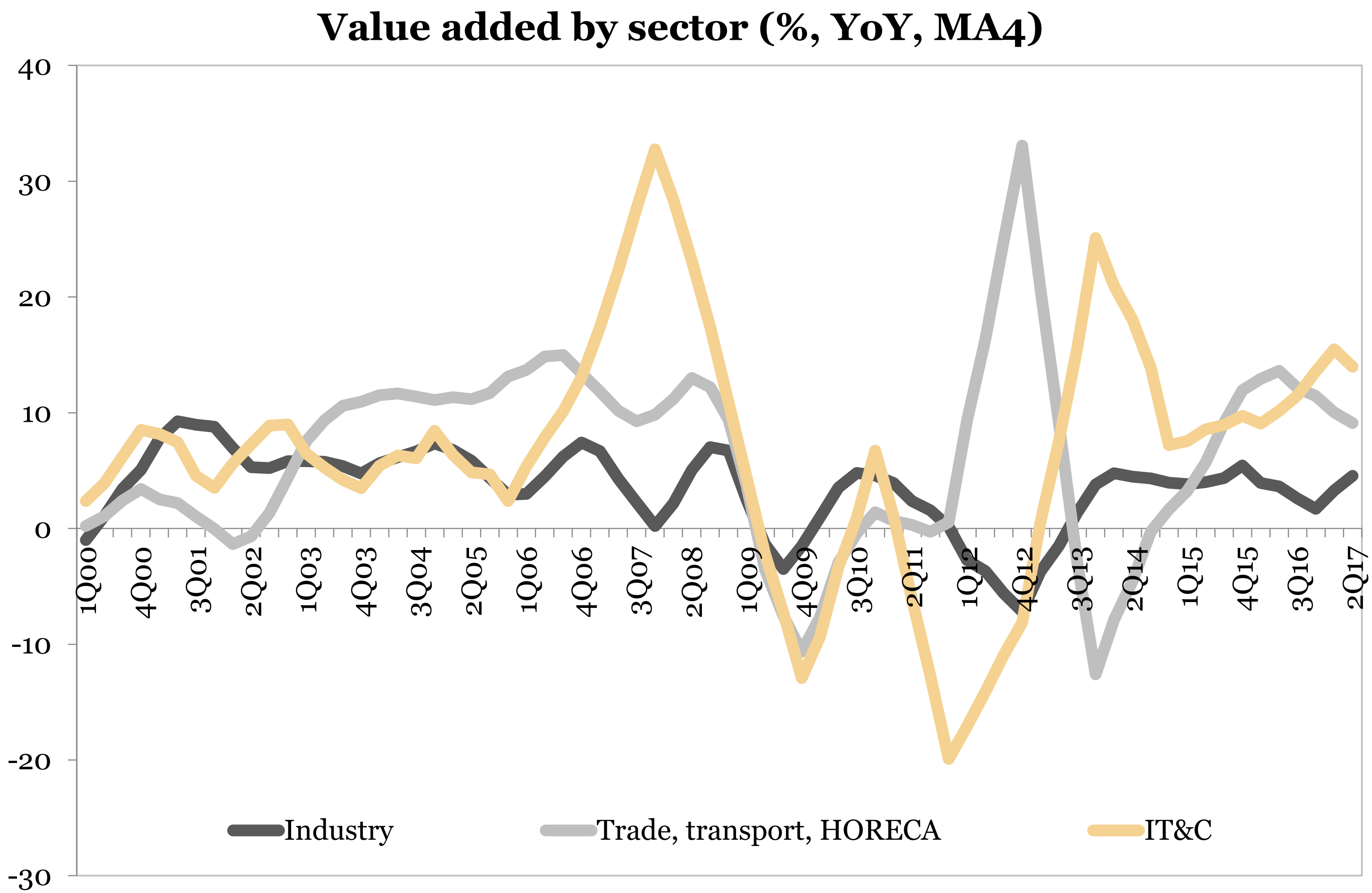
- Romanian GDP accelerated to 5.9% YoY in 1H2017 (and 7% YoY during 9M2017), the highest paces since 2008, evolution supported by the expansionary policy-mix
- Household consumption up by 7.6% YoY, due to the increase of the real disposable income, the dynamics of the credit markets and the wealth effect
- However, the fixed investments contracted by 0.3% YoY in 1H2017, given the increase of the labor costs, the decline of the public investments and the policy-mix related uncertainties and distortions
- Negative contribution of the net foreign demand
- The intensification of the twin deficits
- Unemployment at record low levels
- The inflexion of the YoY CPI dynamics
- NBR ready to start a new monetary cycle

STRONG CONSUMPTION vs. LOW INVESTMENTS



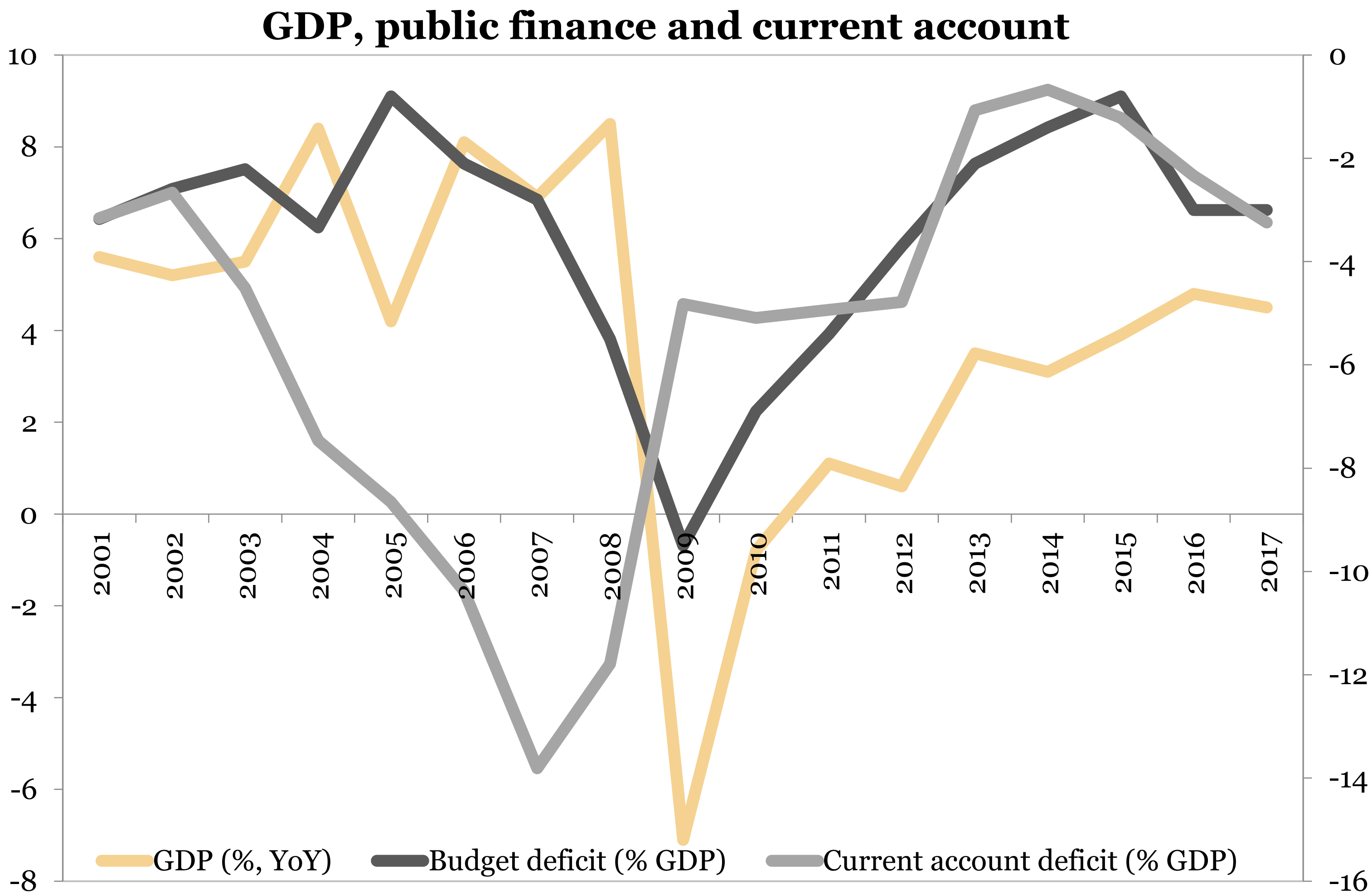
Source: Eurostat, AMECO, INS

IT&C – THE STAR OF THE ECONOMY



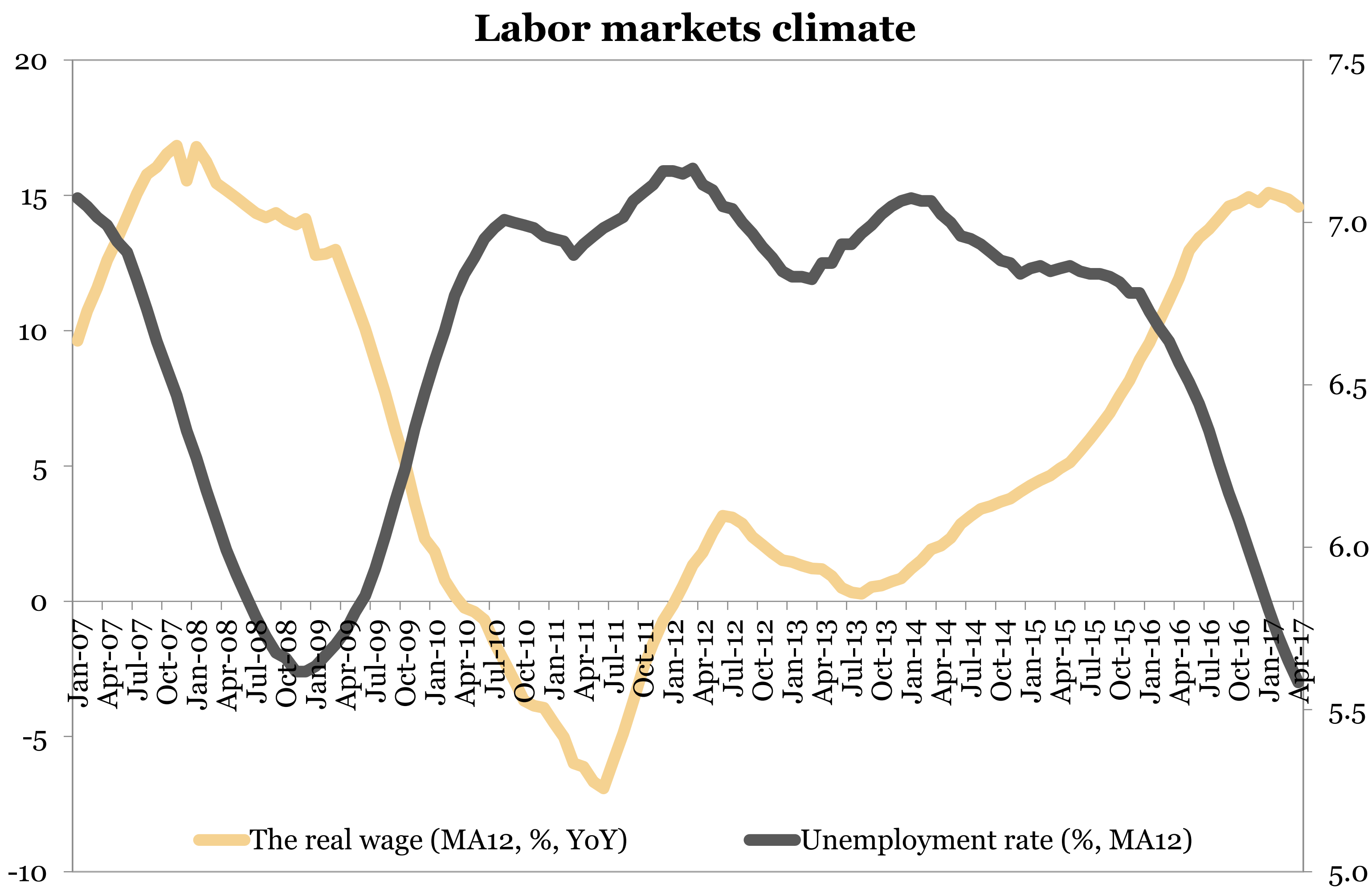
Source: National Institute of Statistics (NIS)

RETURN OF TWIN DEFICITS



Source: AMECO, IMF, Banca Transilvania forecasts

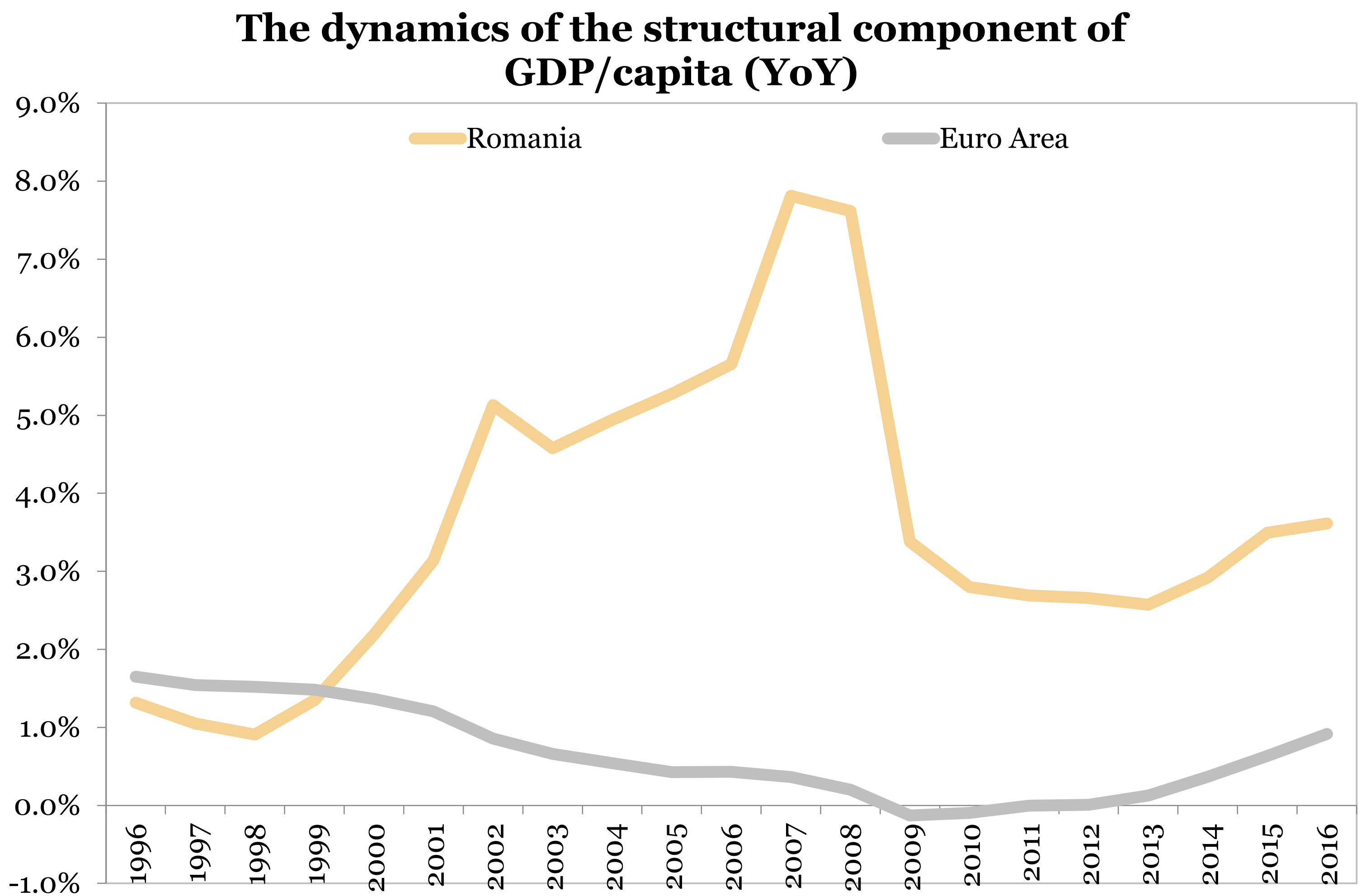
LABOR MARKETS (OVER)HEATING



Source: Romanian Statistics Office (INS), Banca Transilvania estimates

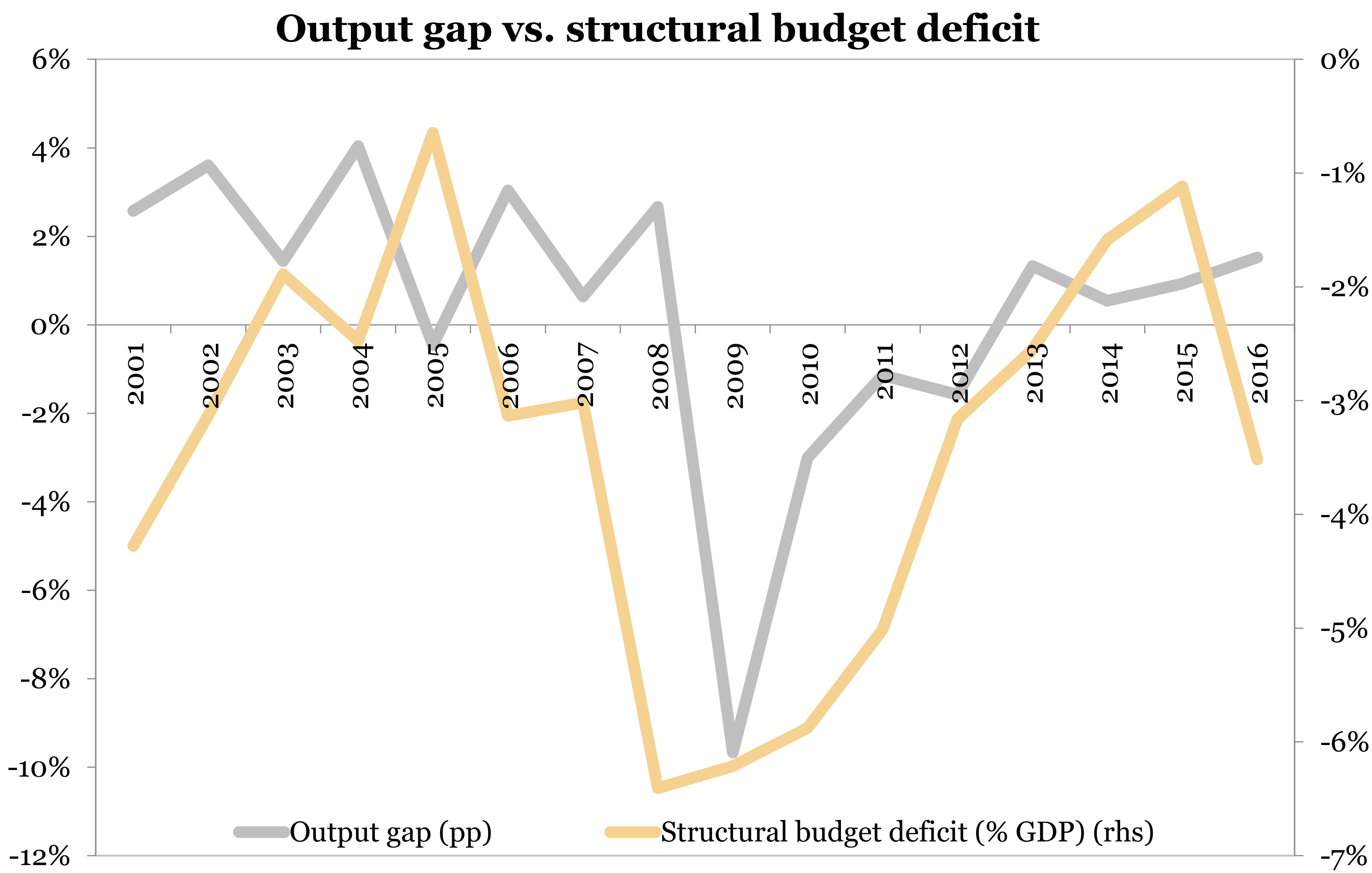
POLICY-MIX IN ROMANIA

CONVERGENCE GOES ON … WITH LOWER PACE



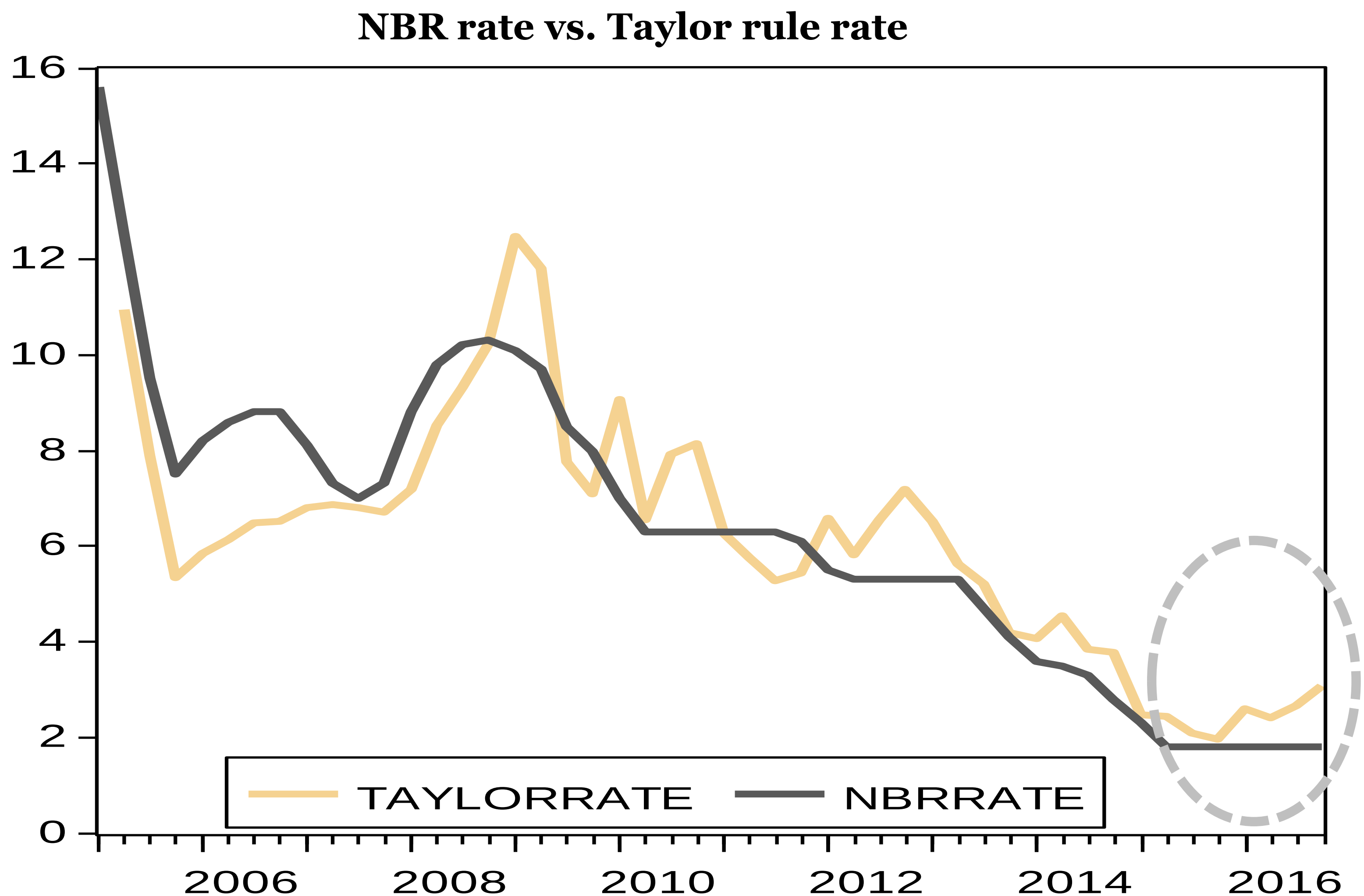
Source: the results of the methodology applied by using data from Eurostat and AMECO

STRONG PRO-CYCLICAL FISCAL POLICY



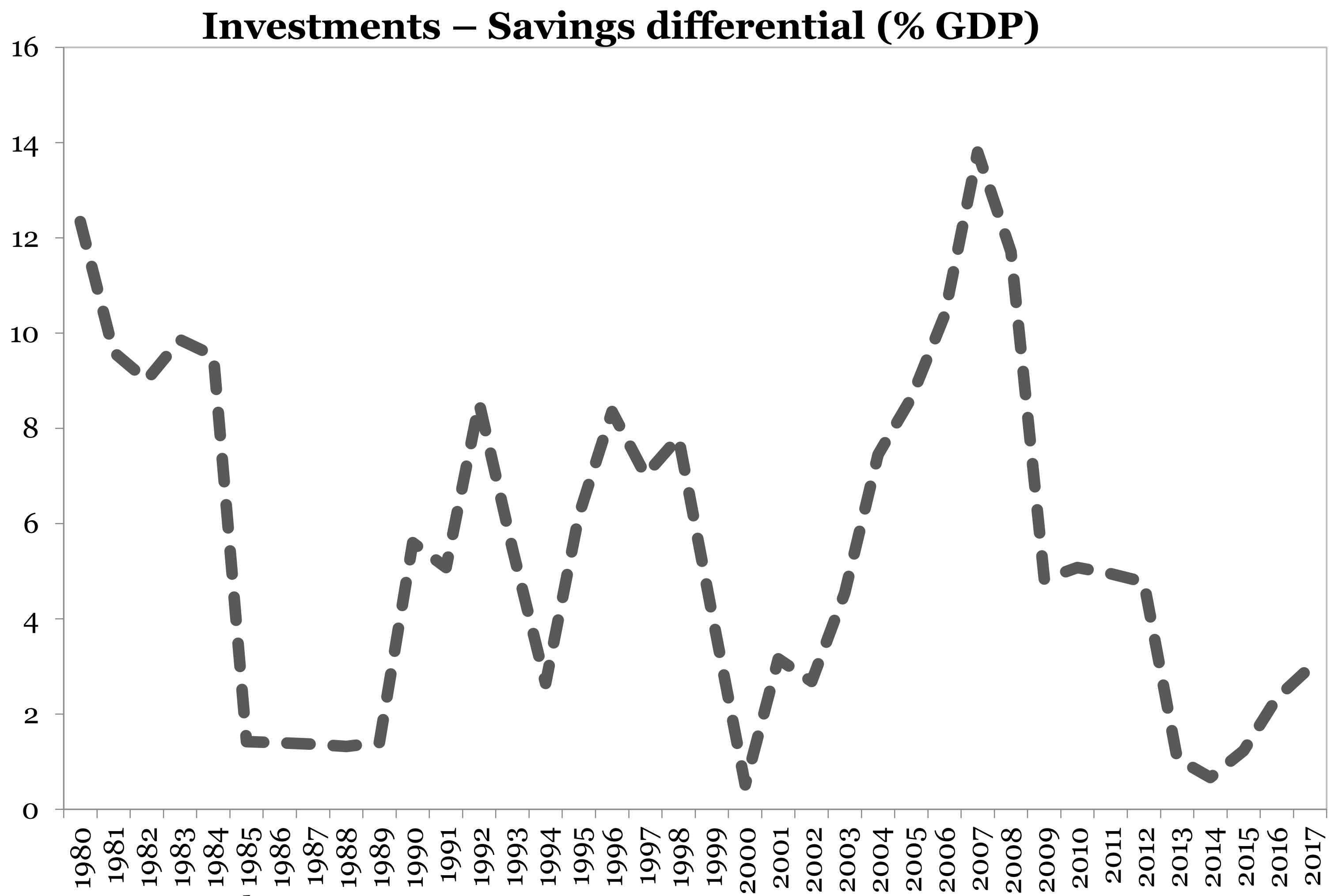
Source: the results of the methodology applied by using data from Eurostat and AMECO

AN EXPANSIONARY MONETARY POLICY



Source: the results of the methodology applied by using data from Eurostat , NBR, Bloomberg

MACROECONOMIC EQUILIBRIA AT RISK AGAIN



Sursa: IMF, October 2017

BT MACROECONOMIC SCENARIO FOR ROMANIA

A LANDING IN SIGHT

Core macroeconomic scenario					
Indicator / year	**2015**	**2016**	**2017**	**2018**	**2019**
GDP (nominal) (EUR, bn)	160.3	169.6	177.6	187.2	199.9
GDP (real) (%, YoY)	4.0	4.6	5.2	4.1	3.4
Private consumption (%, YoY)	5.9	7.4	7.4	5.4	4.5
Fixed investments (%, YoY)	7.4	-3.5	1.3	3.2	2.5
Public consumption (%, YoY)	0.2	4.7	3.5	2.0	1.1
Exports (%, YoY)	4.6	8.3	8.8	6.7	4.3
Imports (%, YoY)	8.0	9.8	8.9	7.1	4.5
Unemployment rate (%)	6.8	5.9	5.1	4.9	5.1
Inflation (HICP) (%, YoY, average)	-0.4	-1.1	1.1	3.1	2.9
Monetary policy rate (%)	1.75	1.75	1.75	3.50	3.25
Budget deficit (% GDP)	0.8	3.0	3.0	3.0	3.0
Public debt (% GDP)	38.0	37.6	38.2	38.0	37.9
Current account (% GDP)	-1.2	-2.3	-3.1	-3.4	-3.4
10 YR interest rate (%)	3.5	3.3	3.9	4.8	5.1
EUR/RON (yearly average)	4.44	4.49	4.56	4.65	4.63

Source: Statistics Office, Eurostat, European Commission, AMECO, BT forecasts

CONCLUSIONS

MANEUVER ROOM NEEDED FOR NEXT CRISIS

- A policy-mix rebalancing needed in order to build maneuver room for the end of cycle
- The financing costs would be higher than forecasted in the mid-run if the rebalancing is postponed
- The degree of freedom in terms of monetary policy is relatively low, due to the strong macro-financial integration of Romania with the Euroland and the high speed of capital flows, in a context of unprecedented expansionary ECB policy
- Without a rethink of the fiscal policy there increases the risks for Excessive Deficit Procedure, with negative consequences for the sovereign rating
- A stronger coordination of monetary and fiscal policies important to avoid boom/bust
- Structural reforms needed for sustainable development and for a successful integration in OECD and Euro Area in the future

THANK YOU!

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