QUALITATIVE ANALYSIS OF THE EVOLUTION OF ROMANIAN ECONOMY IN 2013 AND VALUATIONS FOR 2014

Florin Marian BUHOCIU
Dunarea de Jos University of galati, Romania
florin.buhociu@ugal.ro

This paper has proposed to analyze the evolution of the Romanian economy in 2013 by dynamic levels of significant macroeconomic indicators, namely: industrial production, manufacturing, retail and volume of market services provided to the population, buildings and new car sales. Also the unemployment rate was analyzed. We considered it necessary to present also two indicators rarely used in macroeconomic analysis, namely "the feeling of confidence in the economy" and that of "consumer confidence". They were analyzed also the evolution of certain indicators such as the RON/ EUR exchange rate and that of some regional currencies (PLN, CZK, HUF). Based on the analysis of evolution of all these economic and financial indicators, we could appreciate that the national economy is on an upward trend, with real opportunities to continue the current growth in 2014.

Keywords: economic development, short-term indicators, inflation, key rate, GDP growth, regional exchange rates

JEL Code: O16

1. Introduction

Evaluation of an economy can be achieved by taking into account at least two types of macroeconomic indicators:

1. Development specific indicators,
2. Financial indicators, such as inflation, exchange rate, monetary policy rate.

Based on the dynamics of these indicators in 2013 we will present a qualitative analysis of the evolution of Romanian economy for this period and some feedback on its progress in 2014.

2. Dynamic economic Indicators in 2013

2.1 GDP dynamics

Real GDP expanded by 5.2% in 2013 and 1.7% in Q4 2013, according to flash estimates published by the National Institute of Statistics (NIS). This was substantially above government expectations (2.9% in 2013 and 0.2% quarter) and market consensus (2.8% 2013 and 0.3% quarter). Agriculture is likely to be the main factor that explains faster than expected GDP growth dynamics in Q4 2013, but net exports and industry had a positive contribution, as it was suggested by short-term indicators. Also, households' expenditure and investments probably have increased in Q4 from Q3 2013. According to our estimations, real GDP excluding agriculture expanded also faster than government expectations in Q4 2013, by about 1.8-1.9% yoy. Real GDP increased by 3.5% in 2013, which was also above our expectations (2.7%). In current baseline scenario, the real GDP will advance by 2.3% in 2014(Iancu A.,2011).

Table 1: Dynamics of short-term indicators
Year 2013

Current Issue	Indicators	%quarter			
		Q1	Q2	Q3	Q4
1	Industrial output	2.6	2.0	0.9	3.4
2	Manufacturing output	2.8	4.7	-0.6	2.9
3	Retail sales, real terms	1.0	-1.6	2.0	1.2
4	Turnover in market services for population	-10.6	2.0	9.3	-4.4
5	Turnover in market services for enterprises	5.6	-0.5	4.1	0.1
6	Construction output	-0.9	0.1	8.5	-6.8
7	New passenger cars sales	5.0	-17.1	23.5	2.8

Current Issue	Indicators	%quarter			
		Q1	Q2	Q3	Q4
8	Unemployment rate (%)	5.25	5.20	5.10	5.47
9	Economic sentiment index (level)	95.0	95.6	96.5	95.3
10	Consumer sentiment index (level)	-32.7	-35.8	-35.0	-35.3

Note: Q= quarter of a year
Source: National Institute of Statistics, European Commission, APIA, National Agency for Employment, Raiffeisen Research

Despite the decline recorded in December (-1.1%), industrial output went up by 3.4% quarter in Q4 2013, driven mainly by the positive evolution of Manufacturing (+2.9% qoq). Industrial production increased by 7.1% in 2013, being a key driver of GDP growth. The performance of retail sales ameliorated towards the end of 2013. Retail sales advanced by 0.6% in December and the last quarter of the year showed an increase equal to 1.2% quarter. Looking forward, we consider that this slightly improvement trend in retail sales will continue this year also, helped by the recovery we expect in domestic demand amid a context with accommodative monetary policy. Construction works, on the other hand, decreased by 1.1% in December 2013, resulting in a negative quarterly dynamics equal to -6.8% in Q4. This quarterly shrinkage comes after a major increase recorded in 2013 Q3 (8.5%) and suggests the construction sector had probably a negative contribution to the GDP evolution in 2013 Q4. In annual terms, output in constructions declined by 1.6% in 2013.

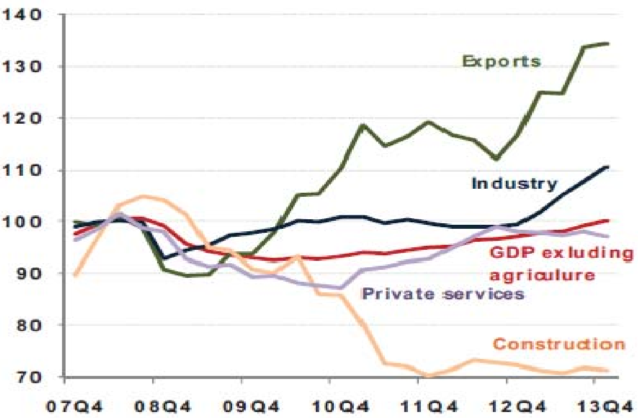
2.2. Agriculture and industry, the key drivers of GDP growth

Agriculture and industry, the key drivers of GDP growth in Q4 2013 (5.2% in 2013 and 1.5% quarter), which surpassed by far market expectations, was determined by the considerable advance of agriculture and industry (Graphic nr. 1).

Agriculture recorded a strong advance of 38.2% in 2013, while industry went up by a considerably 12.6% in year, the contribution of the two sectors, 1.7pp and 3.5pp respectively, explaining entirely the aggregate annual dynamics of real GDP in Q4 2013, equal to 5.2% in year. On the demand side, household private consumption showed a promising positive evolution (3.2% year and 1.4% quarter), with some support from the increase in self-consumption of agricultural products by people living in rural areas. Gross fixed capital formation, on the other hand, declined by 10.8% in 2013 (-5.7%quarter), resulting in a negative contribution to year on year real GDP growth equal to -2.8pp. Inventories improved considerably in Q4 2013, adding up 4.1 pp to annual GDP growth rate. While drop in investments might be also regarded as positive, acting as a buffer that will support further the progress of industrial production(Virlanuta O.,Nechita D., 2013)

Real GDP excluding agriculture, a measure we prefer for tracking short-run tendency of economic activity, displayed also an impressive upward move in Q4 2013 (+3.7% yoy), dwarfing our expectations (1.8% - 1.9%). We maintain unchanged our forecasts for the dynamics of economic activity in 2014 (2.3% for year for real GDP, respectively 2.6% for year for real GDP without agriculture), but in the light of the new data we cannot rule out the possibility of a faster dynamics. This will become clearer when the data on economic activity in Q1 2014 will be released(Dragota V.,Ciobanu A.,Obreja L.,Dragota M., 2003).

Graphic no. 1: Economic activity remains on an upward trend



Source: National Institute of Statistics, Raiffeisen Research
Note: fixed base index, H1 2008 = 100

Industrial production confirmed its ascending trend in January 2014, increasing by 2.3%, on the back of the manufacturing sector, which expanded by 3.4%. Strong advance of industrial output in January 2014 comes after two negative dynamics in November (-0.7%) and December (-0.6% mom). In annual terms, industrial output increased by 9.8% yoy, a pace close to that recorded in December (+10.5%) that bodes well for real GDP growth in Q1 2014. Furthermore, retails sales figures in January 2014 were also a source of positive signals on quarterly GDP performance, posting an increase of 2.4%. The annual dynamics of retail sales (+5.1% in a year), non-food products (+9.7% in a year), fuels (+1.0% in a year). On the other hand, construction works declined considerably in January 2014, by 4.3% (-7.4% in a year), accentuating the negative trend witnessed in previous months. However, the negative evolution of construction sector might not have a significant impact on GDP growth in Q1 2014.

2.3 Dynamic of Economic Sentiment

Economic Sentiment Indicator (ESI) went up by 3 points in February 2014, to 97.7 points. This advance is very important as it follows two consecutive drops and pushers the index at the maximum level from 2013. Confidence in industry, services, retail and building sectors posted an improvement from January and could be a hint that economic recovery might be on an ascending trend in the next period. The consumer confidence index recorded only a minor increase in February 2014, but it was also a tad better that at the end of 2013, emphasizing that full recovery in domestic demand is still sluggish and will probably remain so in the next period(Croitoru L.,2011).

3. Economic evolution in 2014

3.1Inflation evolution

Monthly dynamics of consumer prices stood at 0.3% in February (1.1% in a year), in line with market consensus and close to estimate (0.2%, 0.9% year). We consider that inflation reached its lowest level in February and will start to increase in the subsequent month. A considerable advance will be seen in April, when the introduction of unitary excise of 7 eurocents per liter of fuels will materialize. This tendency (inflation remaining on an upper trend) will be more visible in Q3 when favorable statistical base effects (for example that associated to the VAT cut for bread and related products) will begin to dissipate. The baseline scenario assumes an inflation close 3.5% at the end of 2014, assuming a normal agricultural year; otherwise it could reach greater values(Woodford R.,2001).

CORE3 inflation measure (excluding volatile prices of food products and fuels, administrated prices, alcohol and tobacco) stood at 0.2%, a development suggesting that underlying inflation pressures remain contained. We expect CORE3 measure to register values below 2% at the end of the current year.

Current inflation outlook does not offer room for the central bank to continue with rate cuts, therefore we expect the monetary policy rate to remain unchanged at 3.5%. However, National Bank of Romanian (NBR) could use alternative monetary policy instruments to alter the stance of monetary policy such as management of liquidity in the money market, reduction of Minimum Reserve Requirements (MRR) ratios, as well as narrowing the spread between the interest rate on the permanent credit facility and interest rate on the permanent deposit facility. The reduction of MRR ratios could be on the agenda of the next monetary policy meeting on 28 March, while management of liquidity in the banking system is a measure that can be used on a daily basis by the central bank, but it can be accompanied by increased volatility in money market rates.

3.2. Key rate evolution

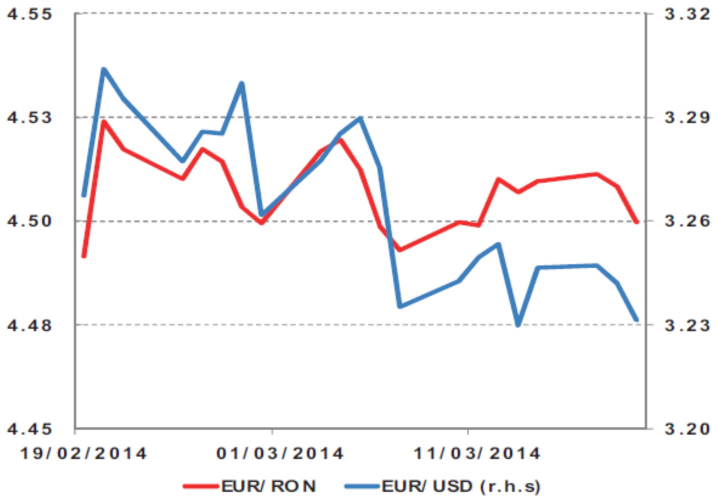
In line with market expectations, the central bank reduced the monetary policy rate by 25bp to 3.5% at the monetary policy meeting at the beginning of February. The key rate cut came in the context of increasing turbulences on the external markets that had the potential to complicate the decision framework. The monetary authority signaled that the key rate cutting cycle might have ended, but the possibility of future reduction in minimum reserve requirement (MRR) ratios at a moderate pace remains. However it might take some time until the next reduction in MRR ratios, since the effect of the previous monetary policy adjustments has yet to be fully incorporated. It is also expected that the National Bank of Romania (NBR) will continue to use the management of liquidity as an effective policy instrument to deal with exchange rate fluctuations, fuelling in this way volatility of the interbank interest rates. In the new issue of the Inflation Report, NBR revised the inflation forecast for the end of 2014, to 3.5%, from 3% in the previous issue, the main reason behind the upward revision being the large increase in excises. Upward revision of inflation forecast to 3.5% and a balance of risks to this forecast that is tilted on the upside, is another argument favoring our view that the central bank would not reduce the key rate further.

4. Recent Exchange rates of RON

Dynamics of leu exchange rate were not notably influenced by developments on the political scene (Graphic nr.2).

However, politics remain a risk factor for the exchange rate in the long run. EUR/RON rate remained somewhat stable in the last two weeks of trading at levels in the range 4.49-4.51. For the next (immediate) period there is no domestic news that could have a strong impact on leu exchange dynamics. In the absence of important shocks from external markets we think the trading level will remain in the interval 4.50 – 4.52.

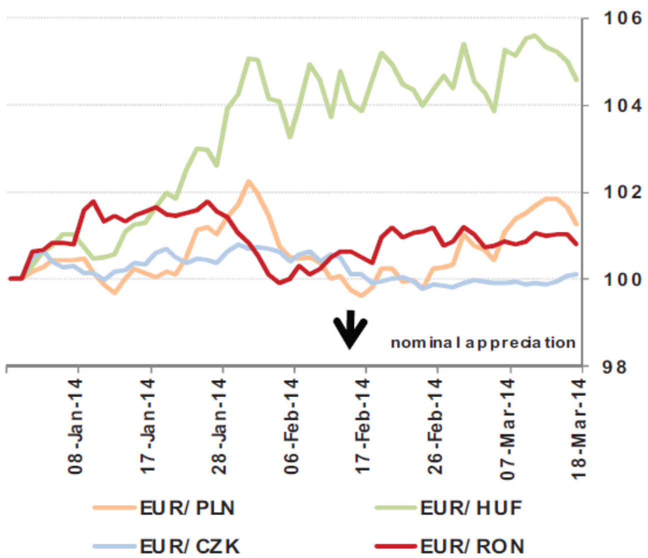
Graphic nr.2: Recent dynamics of RON exchange rate



Source: National Bank of Romania

Also the RON exchange rate in region (Poland,Hungary,Czech Republic) has a good evolution in 2013 and there are good perspectives for 2014(Graphic nr.3).

Graphic nr.3: Regional exchange rates



Source: Reuters Datastream
Note: Fixed base indexes, 31 Dec 2013 = 100

5. Conclusions

The analysis and study of macroeconomic indicators and financial levels presented show that Romania's economy has developed favorably in 2013 and that there are good premises as in 2014 to continue this positive trend. In parallel we must emphasize that there is a trend of increasing confidence in the economic environment on the favorable evolution of the Romanian economy and an increase in the level of consumer satisfaction.

References

1. Croitoru, Lucian Three Unemployment Rates Relevant to Monetary Policy,Romanian Journal of Economic Forecasting,Vol. XIV,no. 3/2011,Institute for Economic Forecasting
2. Woodford,Michael Inflation Stabilization and Welfare,Working Paper 8071,NBER(January),2001
3. Iancu, Aurel Models of Financial System Fragility,Romanian Journal of Economic Forecasting No. 1,2011
4. Dragota V., Ciobanu A.,Obreja L., Dragota M. Management Financiar, Editura Economica Bucuresti 2003
5. Virlanuta,O., Nechita Daniela – The Mutual Investments in Romania – Current Developments and Trends –Annals of „Dunarea de Jos" University of Galati, Fascicle I. Economics and Applied Informatics, year XIX, nr.1/2013, ISSN 1584-0409, pg. 73-76
6. www.bnr.ro