REGIONAL ECONOMICS & MARKET STRATEGY MONTHLY

February-March 2018

Bulgaria | Cyprus | Romania | Serbia

Ioannis Gkionis
Senior Economist
Eurobank Ergasias
+30 210 3331225
igkionis@eurobank.gr

Galatia Phoka
Research Economist
Eurobank Ergasias
+30 210 3718922
gphoka@eurobank.gr

Regional assets broadly rebound from February's sell-off

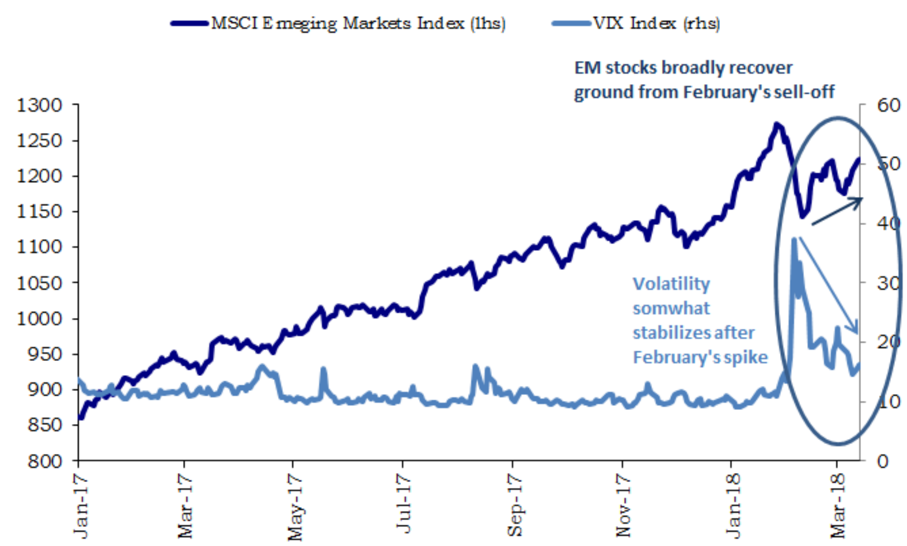
REGIONAL MACROECONOMIC & MARKET DEVELOPMENTS & OUTLOOK

- **Q4 national accounts releases** more or less in line with expectations. Regional growth **prospects** still look very good in **2018**
- Real disposable incomes are expected to continue rising albeit at a lower speed compared to last year, thereby providing support to **private consumption**
- The rise of **investments** is crucial for the **medium-term** growth prospects of the region
- **Different** inflation paths allow for **divergent** regional Central Banks' monetary policies
- **Regional stock markets mostly recoup** some losses
- **Regional currencies remain little changed** with idiosyncratic factors mostly at play
- **Local currency sovereign bonds mostly weakened** over recent weeks; **FX denominated T-bonds** retained YTD gains
- **EM asset prospects remain positive** but risks lie ahead

COUNTRY FOCUS

- **Bulgaria:** Investments performance is key to a more balanced growth path in 2018
- **Cyprus:** Presidential elections results signal policy continuity
- **Romania:** Elevated inflationary pressures amid lower growth
- **Serbia:** Real GDP growth to pick up this year after supply-side shocks slowdown in 2017

EM assets recover some ground after February's sell-off



Source: Bloomberg, Eurobank Research

Contents

I. Regional Macroeconomic & Market Developments & Outlook

Divergent Central Banks' monetary policies in 2018; regional assets recovering after February's selloff

Different inflation paths allow for divergent regional Central Banks' monetary policies

The national accounts releases of Q4-2017 confirmed that the economies of the region have had the best year in the post-Lehman period last year. Growth prospects still look very good for most of the economies in 2018. Private consumption is expected to make a key-yet smaller than last year- contribution to GDP growth. A favorable external environment will allow those small open economies maintain their net exports contribution in check next year despite the uptick on the imports side. Nevertheless, it is going to be investments whose performance should make the difference both this year and in the medium-term. More importantly, the region's EU funds absorption, which has failed to impress in the past two years for a number of reasons, is expected to accelerate providing a boost to public investments. The outlook looks more challenging from a policymaking point of view, as lax monetary policies from both major and regional central banks have embarked on a normalization course which is expected to unfold fully in 2018. Yet, the rising trend of core and headline inflation metrics is uneven across the region allowing for different degrees of freedom in the respective CBs' monetary policies. The majority of CBs in the region maintain their cautiously accommodative stance. On the other hand, Romania is an outlier. NBR has already delivered two hikes of 25bps in the first two months of the year bringing the KPR at 2.25% given the inflation (expectations) jump.

EM assets broadly recovered some ground after February's selloff

Emerging market assets broadly recovered some ground after a choppy February. Volatility seems to have somewhat stabilized over recent weeks and the view about a predictable and gradual monetary policy normalization by major Central Banks in tandem with strong global growth this year continues to prevail. Some renewed bouts of risk aversion were instigated primarily by concerns over US trade protectionism and uncertainty surrounding US policies following the dismissal of key US administration personnel.

Emerging market stocks mostly recoup some losses but remain below 2018 highs

Regional currencies remain little changed with idiosyncratic factors mostly at play

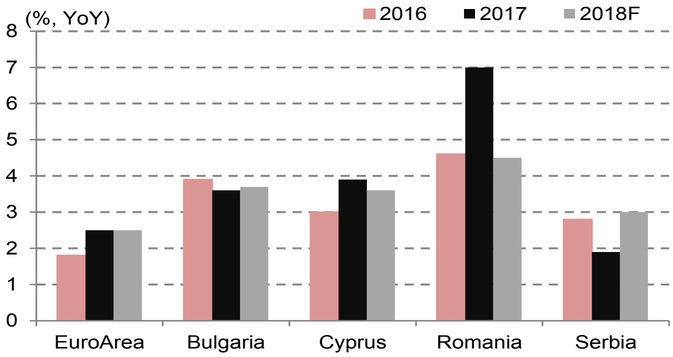
Having recouped some of the hefty losses incurred last month, which saw the index decline by more than 10% from a decade peak reached in late January, the broad MSCI EM index has firmed about 8% from 1 ½ month lows reached on February 9, to currently stand nearly 6% firmer on a year-to-date (YTD) basis. Main indices in the countries of our focus have recovered from early February lows, but most stand weaker from recent 2018 peaks. That said, Romania's BETI has outperformed its regional peers with an 11.0%YTD advance to stand at a 9-month peak in mid-March. In the FX markets, regional currencies currently trade little changed YTD, despite the US dollar's weakness. Idiosyncratic factors, in many cases ultra-loose monetary policies, are being mostly at play. After reaching 3 ½ year highs just below 118.00/€, the Serbian dinar eased to 2-week lows to stand flat YTD after a weak inflation reading in February and an ensuing rate cut in the key policy rate. The Hungarian forint has also remained under pressure standing modestly weaker year-to-mid-March and having hit a 2 ½ month low at 314.40/€ in late February as the Central Bank continues to purse ultra-loose monetary policy via the introduction of unconventional instruments as of this year. The Turkish lira hit a record low slightly above 4.81/€ in the wake of a Moody's downgrade in early March, increased political uncertainty following the passage of a controversial elections law, increased tensions in the country's relations with the US and the EU, a high current account deficit and the lack of a more aggressive Central Bank action despite elevated inflation. In the local currency sovereign bond markets, local government bonds have mostly weakened recently, while FX-denominated T-bonds mostly retained YTD gains.

EM asset prospects remain positive but risks lie ahead

Looking ahead, the risk environment echoes rather cautiously positive for emerging market assets, thanks to improved macro fundamentals, synchronized global growth and narrowing external imbalances and are admittedly in a much better position to withstand monetary policy normalization by major Central Banks and increased bouts of risk aversion. That said, valuations in some asset classes, particularly equities and credit, appear rich following the strong rally in the last two years. On the other hand, a flurry of risks lie ahead, such as a more protectionist trade policy from the US, a sharper than expected slowdown in China, higher than anticipated inflation and ensuing faster than expected monetary policy normalization from major Central Banks, weaker than expected global growth, geopolitical events and a heavy political calendar in EMs.

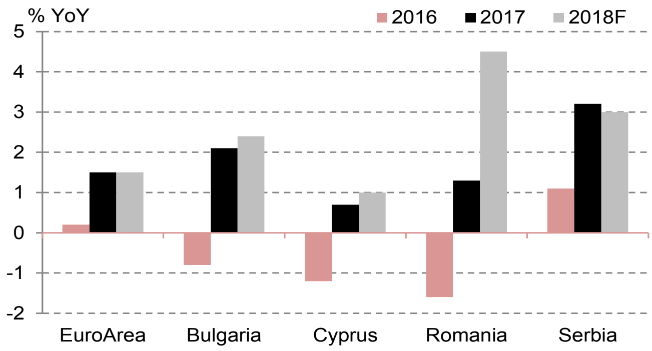
Ioannis Gkionis (igkionis@eurobank.gr)
(+30) 210 337 1225
Galatia Phoka (gphoka@eurobank.gr)
(+30) 210 371 8922

FIGURE 1: GDP Growth performance 2016-2018



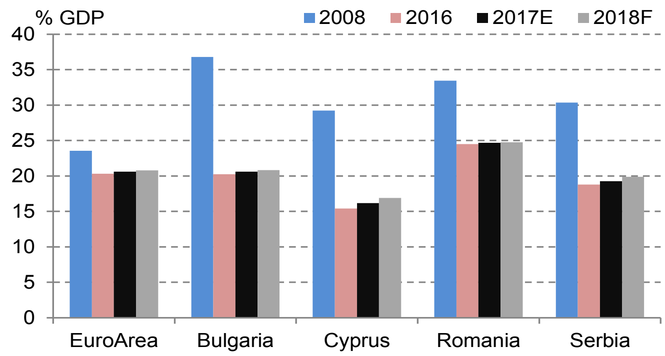
Source: Eurostat, National Authorities, Eurobank Research

FIGURE 2: Annual average inflation 2016- 2018



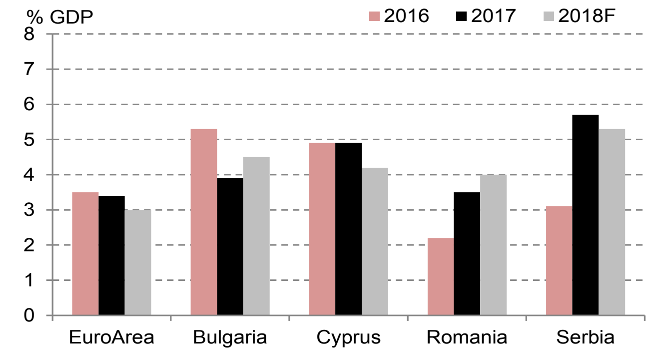
Source: Eurostat, EU Spring Forecasts, Eurobank Research

FIGURE 3: Investments to GDP ratios 2008 vs. 2018



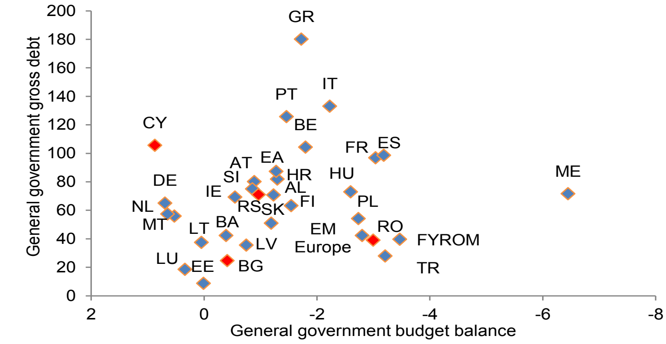
Source: IMF WEO, Eurobank Research

FIGURE 4: Current Account Balance (% of GDP) 2016-2018



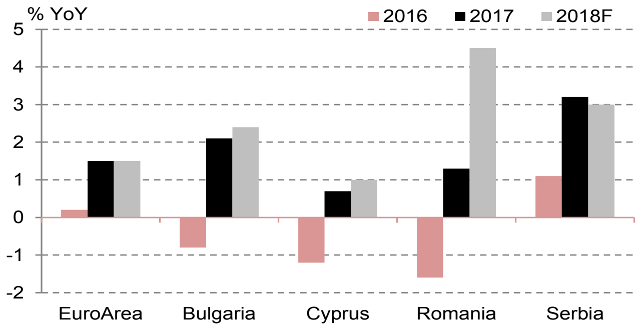
Source: Eurostat, National Authorities, Eurobank Research

FIGURE 5: Fiscal Balance & Public Debt (% of GDP, Cash basis) 2017



Source: IMF National Authorities, Eurobank Research

FIGURE 6: Annual average unemployment rates 2016-2018



Source: Eurostat, National Authorities Eurobank Research

FIGURE 7: Major world & CESEE stock markets performance (%)

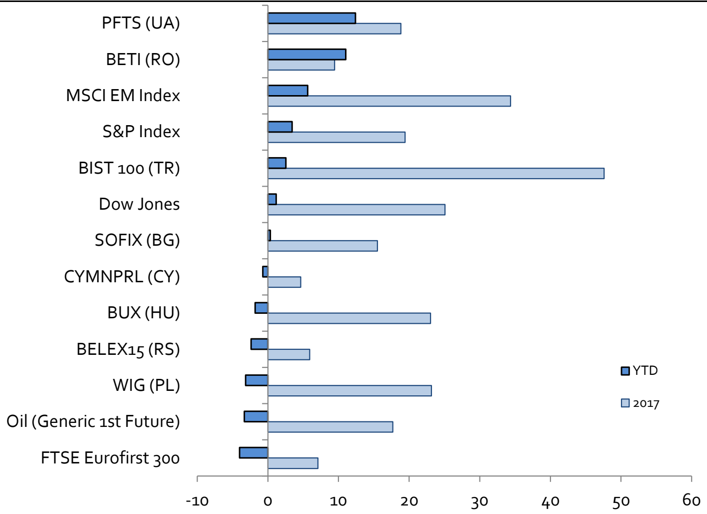


FIGURE 8: World & EM stock markets performance

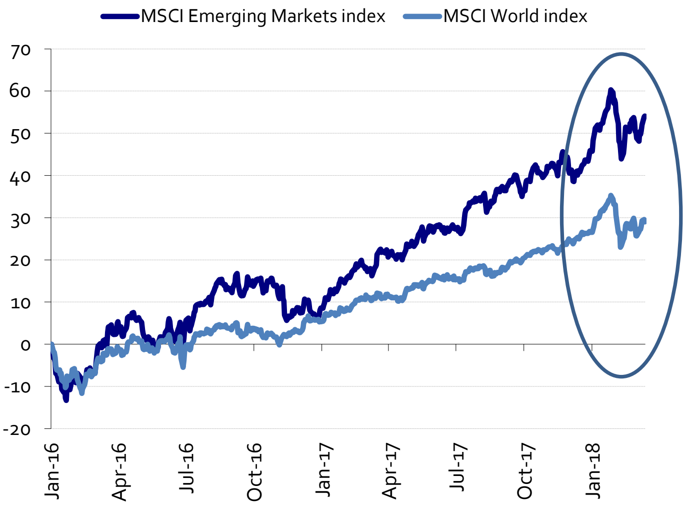


FIGURE 9: MSCI stock indices performance (by region)

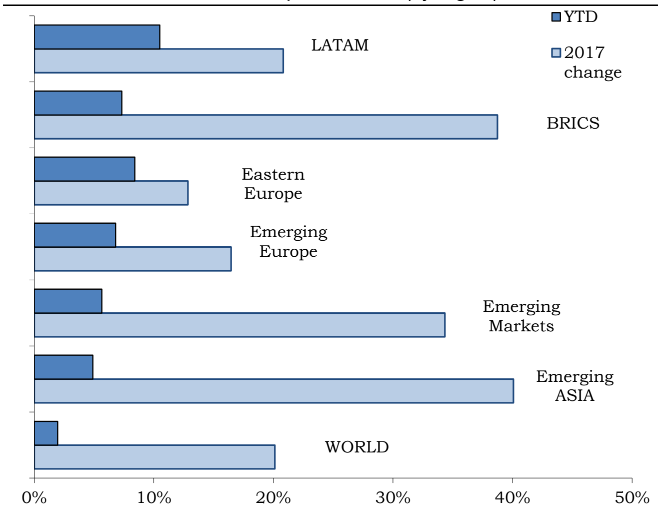


FIGURE 10: CESEE FX performance

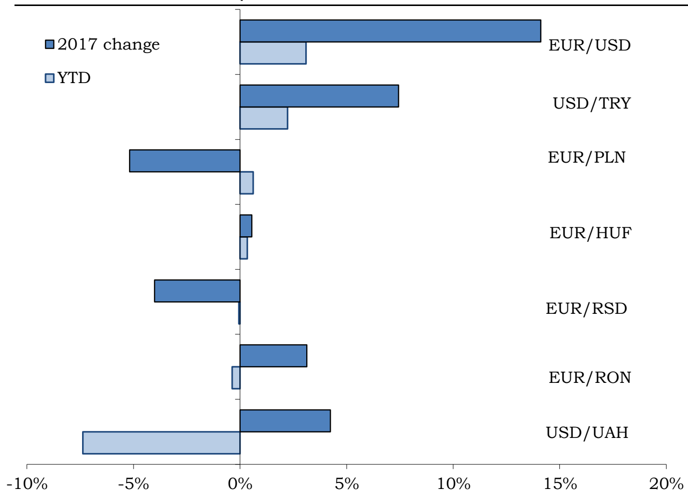
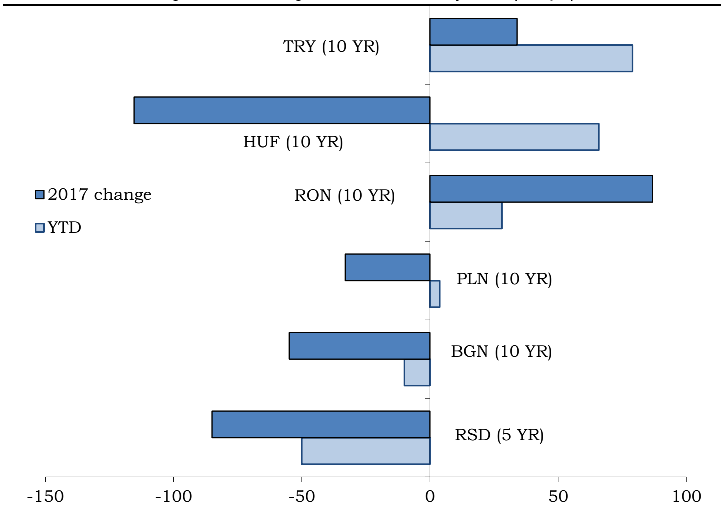
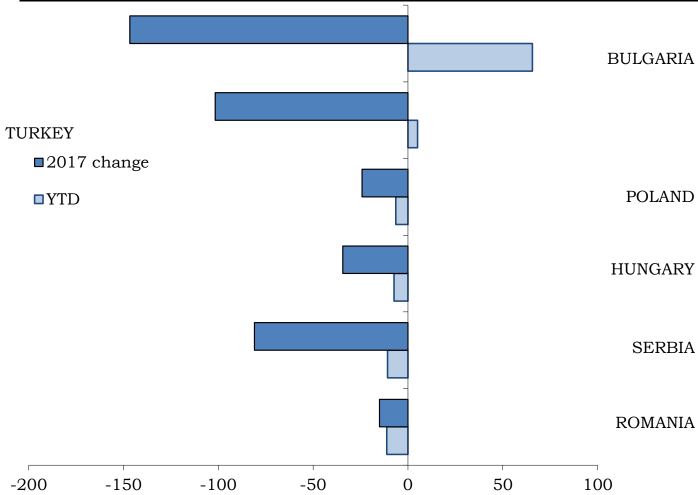


FIGURE 11: Change in CESEE government bond yields (in bps)



Source: Reuters, Bloomberg, Eurobank Research

FIGURE 12: Change in 5-Year CDS spreads (in bps)



Source: Reuters, Bloomberg, Eurobank Research

Trader's view

FX

Risks remain tilted towards further upside for the dinar

Our earlier conviction for further dinar gains in the coming weeks/months has been vindicated since late January. The RSD indeed firmed to new 3 ½ year highs just below 118 against the euro as the National Bank of Serbia (NBS), intervened repeatedly in the FX markets with daily purchase of €30mn on average to alleviate ongoing appreciation pressures on the currency. Even so, risks remain tilted towards further upside for the dinar as demand for Serbian RSD T-bonds (SERBGB), which appears to be the biggest driving force behind the dinar's appreciation momentum over the last few weeks, is likely to continue unabated. This holds especially as the bond auction schedule for March remains heavy (with the 5Y or 10Y bond offered on auction every Tuesday). In addition, we remain bullish on government bonds as well. Despite the occasional global jitters, and uncertainty surrounding the pace of monetary policy normalization by the ECB, SERBGBs still have room to perform well throughout 2018. Several reasons stand behind this argument. Firstly, the easing Central Bank cycle may have not yet reached its bottom, with another rate cut aimed at supporting the economic recovery still echoing possible. The country's public debt has embarked on a sustainably downward trajectory. Further EU accession progress also bodes well with lower borrowing costs, while a new IMF program, of an advisory nature such as PCI, will pave the way for further rating improvements and provide additional safety to new foreign investments. The potential future inclusion of Serbia's sovereign debt into the JPMorgan GBI-EM bond index, as part of Public Debt Administration's efforts, will enhance secondary market liquidity and transparency/attainability to such Serbian securities.

Local rates

We prefer to remain on the sidelines on Bulgarian bond trades

Bulgarian local-currency bonds have stayed well supported since the beginning of 2018. The sovereign yield curve experienced some modest increases on both the short and long end, with the 7 and 8 year tenors exhibiting the largest spikes of ca 6 bps each, while that of 9 year tenor marginally declined in February, by ca 2 bps. The Bulgarian Ministry of Finance did not hold any auctions in February and has also not given any indication of offering any government bonds in March either.

Meanwhile, Eurobond yields continued to rise in February across the board, with shorter maturities such as 2023 and 2024 rising by 9 bps as well as longer ones such as the 2027 and 2028, which jumped by 10 bps. All in all, we currently believe that Bulgarian credit spreads remain tight and valuations continue to be stretched, which is the reason why we prefer to remain neutral and not enter any new positions.

Ruslan Raychev (RSRaychev@postbank.bg)
+359 2 8166 482

Zoran Korac (zoran.korac@eurobank.rs)
+381 11 206 5821

We would also like to the Eurobank Trading Team in Athens for its most valuable comments

II. Country Focus

Bulgaria (Baa2/BB+/BBB-)

Investments performance is key to a more balanced growth path in 2018

Real GDP growth came at 3.5% YoY in Q4 bringing the FY2017 at 3.6%

The Q4 2017 revised GDP growth estimate was trimmed by 0.1ppts on an annual basis from a flash reading, with economic activity coming in at 0.7% QoQ/3.5% YoY down from 0.9% QoQ/3.9% YoY in Q3-2017 and 1.1% QoQ/4.0% YoY in Q4-2016. From the demand side, growth remained driven by still strong final consumption dynamics (+1.3% QoQ/+3.8% YoY in Q4 vs. 0.9% QoQ/+4.3% YoY in Q3). On the positive side, investments were in the black for the third consecutive quarter (GFCF: +0.2% QoQ/+4.5% YoY in Q4 vs. -0.4% QoQ/+4.3% in Q3 vs. +2.6% QoQ/+3.9% YoY in Q2 vs. +2.1% QoQ/-2.6% YoY in Q1). The rise mirrors partial progress in infrastructure spending implementation after the transition period of the caretaker government and gradual improvement in the EU funds absorption in the two-years after the closing of the previous programming period 2007-2013. On the negative side, net exports were in deep red as imports growth outpaced concomitant increases in exports. In more detail, imports accelerated to 4.4% QoQ/8.3% YoY in Q4 up from 1.3% QoQ/5.1% YoY in Q3 in response to strong private consumption dynamics. Exports decelerated sharply to -1.0% QoQ/+2.0% YoY in Q4 vs. +3.0% QoQ/+4.1% YoY in Q3.

The key to a more balanced growth path in 2018 depends heavily on investments performance

Having expanded by 3.6% YoY in 2017, Bulgaria is now expected to register another year of strong above-potential growth. The economy is expected to benefit from further labor market tightening, accelerating credit activity dynamics, a more expansionary fiscal policy stance, a vibrant export oriented manufacturing sector and an emerging tourism destination. The economy is operating at or close to full employment to the extent that companies are reportedly increasingly confronted with labor scarcity (the relevant % of companies in EU survey has climbed to 40% in Q4 up from only 13% in Q4-2013). The unemployment rate declined further down to 6.1% in Q4-2017 from 6.8% a year ago, the lowest level since Q1-2009. Fiscal policy is expected to be more growth-supportive provided that budget execution aligns with the 1% of GDP deficit target in 2018 vs. a 0.8% surplus in 2017. Credit to the non-government sector accelerated to 4.8% YoY in 2017 vs. only 1.5% YoY in 2016, compared to -1.2% YoY in 2015. Financial institutions are now less reluctant to lend helped by abundant liquidity conditions, as heavy regulatory requirements are behind, and are still confronted by the negative interest rates on excess reserves. With capacity utilization standing at an all-time high, private companies will need to invest more in order to strengthen their productive capacity. In the past year, public investments also fell short of expectations mirroring the inability of the caretaker government and the limited progress by the incoming government coalition to push for infrastructure projects implementation. Finally, investments are going to receive support from improved EU funds absorption.

Although most of the nominal convergence criteria are currently satisfied, real convergence criteria are not

Real convergence criteria are not satisfied, although officially these are not part of the evaluation procedure. The country is still subject to the Co-operation and Verification mechanism, which was set up in 2007 to monitor progress in the fields of judicial reform, corruption and organized crime. Factoring in the fast GDP growth trajectory in 2015-2018, GDP per capita in PPS terms will have only climbed to around 50% in 2018. Finally, IMF in its latest Article IV report sees GDP growth moderating to 2.75% over the medium-term, reflecting capacity constraints and unfavorable demographics.

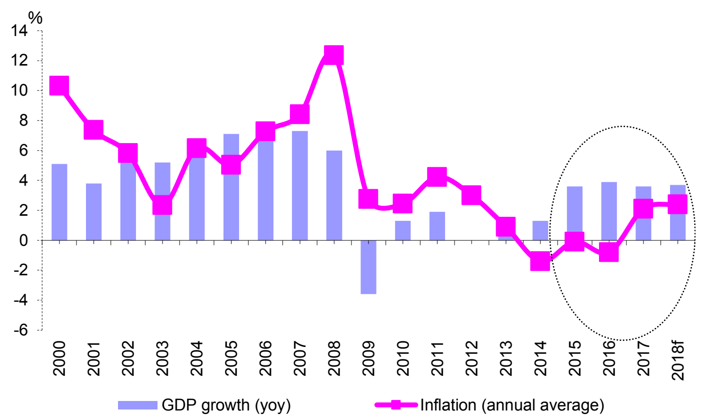
Ioannis Gkionis (igkionis@eurobank.gr)
(+30) 210 337 1225

Bulgaria: Macro & Market Data

Macro indicators	2016	2017	2018f
Real GDP (yoy, %)	3.9	3.6	3.7
Inflation (yoy%, avg)	-0.8	2.1	2.4
Fiscal Balance (%GDP, Cash basis)	1.6	0.8	-1.0
Gross Public Debt (%GDP, Cash basis)	27.8	24.5	24.1
Unemployment Rate (LFS, %)	7.6	6.3	6.0
Compensation of employees/head	3.9	4.1	4.5
Current Account (% GDP)	5.3	3.9	4.5
Net FDI (EUR bn)	0.6	1.0	1.0
Domestic Credit	**2015**	**2016**	**2017**
Total Credit (%GDP)	57.1	54.6	53.1
Private Sector Credit (yoy)	-1.2	1.5	4.8
Loans to Deposits (%)	78.2	74.1	73.1
Financial Markets	**3M**	**6M**	**12M**
Policy Rate		(Currency Board)	
EUR/BGN	1.96	1.96	1.96

Sources: National statistics, Eurostat, IMF, Ecowin Reuters, Eurobank Research

FIGURE 13: GDP growth & Inflation 2000-2018



Cyprus ((P) Ba3/BB+/BB)

Presidential elections results signal policy continuity

The incumbent President was re-elected in the second round renewing his mandate for another 5 year-term

Incumbent President Nikos Anastasiades, backed by the ruling right-wing DHSY, won, as was broadly anticipated, in the 2nd round of Presidential elections. He received 55.9% of the vote, securing another 5-year term in office. The runner up, Stavros Mallas, who was backed by left wing AKEL scored 44.01%. The voters' turn-out in the second round stood at 73.97%, a tad above the first round's historical low of 71.88%. Given that the government system is Presidential, his re-election gives him a strong mandate to pursue the current government policies and ensures policy continuity. On the other hand, given that no party enjoys absolute parliamentary majority, the new President will have to achieve concessions from other parties in the 56-seat parliament in order to pass legislation. The ruling right-wing DHSY controls only 18 seats while DHKO can no longer be counted as a government partner which explains at large the lower re-election approval rate of President Anastasiades. This is not very reassuring given that there is a number of important pending structural reforms in the areas of privatizations, public and health sectors, while addressing the challenges of a still high bad loans stock (NPEs ratio at 43.7% in November 2017) in order to avoid backtracking on the economy.

In Q4-2017 the economy expanded by 3.9% on an annual basis, bringing the FY2017 performance to 4.0%-the highest growth in the post-Lehman period- up from 3% in 2016 and 2% in 2015

The second and latest estimate of CYSTAT about the seasonally adjusted Q4 GDP reading confirmed the flash estimate of 1.2% QoQ/3.9% YoY bringing the FY2017 performance to 4.0%, the highest growth in the post-Lehman period- up from 3% in 2016 and 2% in 2015. This strong quarterly reading compares to 0.8% QoQ/3.8% YoY in Q3-2017, 0.8% QoQ/3.7% YoY in Q2-2017 and 1.1% QoQ/4.1% YoY in Q1-2017, up from 1.0% QoQ/3.9% YoY in Q4-2016. Real GDP growth marked the eleventh consecutive positive reading on a both quarterly and annual basis after a previous three-year recession. The GDP growth rate of Q4 is among the highest in EA-19 and EU-28, both on a quarterly and an annual basis and, for an eleventh consecutive quarter in a row, above that of EA-19. GDP growth is expected to decelerate to 3.6% in 2018 driven primarily by private consumption again. The ongoing consumption rebound is driven by sustained sentiment improvement, a flourishing tourism sector, improved labor market conditions, further property market stabilization, the impact from the fiscal relaxation, and the further normalization of banking sector conditions.

Total bank deposits recorded the highest net monthly decrease since September 2015 in January

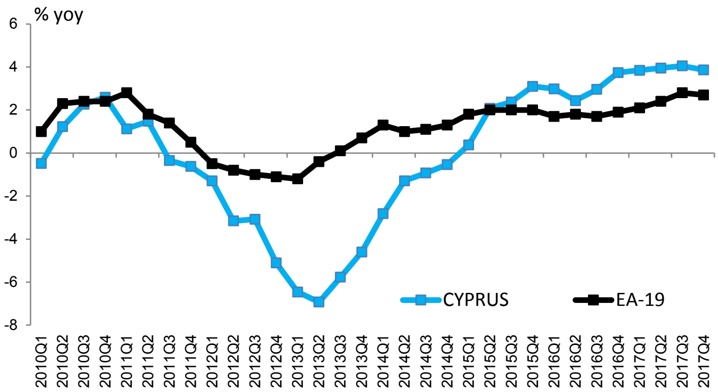
From a flow point of view, total deposits recorded a substantial net decline of €557.1mn in January on top of a net increase of €259.0mn in December, up from a net decrease of €96.4mn in November and a net increase €335.1 in October. The annual rate of expansion-which has been in positive territory since October2015- has slowed down to 1.7% YoY in January down from 3.1% YoY in December and 2.4% YoY in November compared to 6.2% YoY in Dec2016 and only 0.2% YoY in Dec2015. The outstanding amount of total deposits had reached as of October the highest level in the post-MoU era. Total deposits stood at €48.6bn in January down from €49.4bn in December vs. €49.5bn in October compared to €49.0bn in December 2016 and €45.97bn in December 2015.

Ioannis Gkionis (igkionis@eurobank.gr)
(+30) 210 337 1225

Cyprus: Macro & Market Data			
Macro indicators	**2016**	**2017**	**2018f**
Real GDP (yoy, %)	3.0	3.9	3.6
HICP Inflation (yoy%, avg)	-1.2	0.7	1.0
Fiscal Balance (%GDP, Cash basis)	0.4	1.9	1.3
Gross Public Debt (%GDP, Cash basis)	107.8	99.0	92.4
Unemployment Rate (LFS, %)	13.1	11.1	10.0
Compensation of employees/head	-0.6	0.7	1.1
Current Account (% GDP)	-4.9	-4.9	-4.2
Terms of Trade (of Goods)	-0.4	0.2	-0.5
Domestic Credit	**2015**	**2016**	**2017**
Total Credit (%GDP)	360.8	308.3	267.3
Credit to Enterprises (%GDP)	151.5	125.3	107.8
Credit to Households (%GDP)	136.4	127.5	112.7
Private Sector Credit (yoy)	-3.4	-11.0	-7.1
Loans to Deposits (%)	136.6	112.6	103.9

Sources: National statistics, Eurostat, IMF, Ecowin Reuters, Eurobank Research

FIGURE 14: GDP growth performance Cyprus vs. EA-19 2010-2017



Romania (Baa3/BB+/BBB-)

Elevated inflationary pressures amid lower growth

Headline inflation has surpassed the upper bound of the NBR's target interval on supply side factors and base effects

Consumer prices jumped to +4.3% YoY in January up from 3.3%YoY in December, above consensus (4.1% YoY). The said rise was mainly driven by higher food prices on a monthly basis (+0.6% MoM/+4.1% YoY) reflecting the upward trend of volatile fruits and vegetables, the new regulated price increase for energy tariffs (as of January 2018) plus the base effects from the phasing out of last year's VAT rate cut. January's year on year increase is the highest in the last 4.5 years. Headline inflation has now surpassed the upper bound of the NBR's target interval (2.5+1%). The adjusted Core CPI (excluding administered, volatile prices, alcohol and tobacco) advanced further to 2.8% YoY in January compared to December, the highest level since August 2013, in an illustration of building underlying demand side pressures.

The weaker than expected growth reading of the last quarter predisposes for a further slowdown in the period ahead

The revised estimate on the seasonally adjusted Q4-2017 GDP reading confirmed the flash estimate for growth of +0.6% QoQ/+7.0% YoY; +6.9% YoY in unadjusted terms. The weaker than expected print, which came in below a market consensus of +1.2% QoQ/+7.3% YoY, compares with increases of 2.4% QoQ/8.5% YoY in Q3-2017 and 2.1% QoQ/5.0% YoY in Q4-2016. On the demand side, growth was remained driven by domestic demand. Private consumption growth continued running at double digits on an annual basis underpinned by the rise in disposable incomes and further labor market tightening. In more detail, private consumption expanded by +1.8% QoQ/+11.9% YoY in Q4-2017 vs. +3.2% QoQ/+11.6% YoY in Q3-2017 compared to +1.6% QoQ/5.6% YoY in Q4-2016, making a hefty contribution of 6.8ppts to economic activity. Importantly, the investments' rebound continued in Q4. Gross fixed capital formation (GFCF) expanded by +3.7% QoQ/+12.2% YoY in Q4-2017 vs. +2.8%/+6.9% YoY in Q3-2017 having recovered significantly from contraction of 1.2% QoQ /12.4% YoY in Q4-2016. GFCF received support primarily from private investment-from both residential construction and machinery equipment-as public investments failed to impress for yet another quarter reflecting low EU funds absorption and the under-execution of the public investments program as a means to contain the fiscal deficit at the expense of neglecting infrastructure. Meanwhile, net exports had a negative contribution of 1.5ppts to growth in Q4 mirroring the faster expansion of imports (1.1% QoQ /+10.4% YoY in Q4 vs. 0.1% QoQ/+11.1% YoY in Q3) against that of exports (+1.3% QoQ/+7.2% YoY in Q4 vs. +2.1% QoQ/+9.0% YoY in Q3).

A sharp growth slowdown in on the cards in 2018

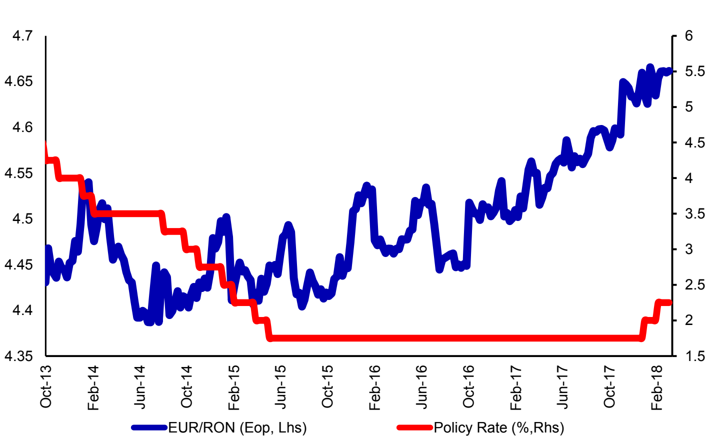
Real GDP expanded by 7.0% in 2017 compared to 4.8% in 2016, outperforming regional peers for the fourth consecutive year and surpassing the most optimistic forecasts. Growth remained largely driven by private consumption, financed by an overly expansionary fiscal policy, which has led to a revival of macroeconomic imbalances (CAD17: -3.5% of GDP). A sharp slowdown to 4.5% is on the cards in 2018 reflecting the impact of higher inflation-above the NBR target band-on real disposable incomes, front-loaded monetary policy and the need for a more conservative fiscal policy.

Ioannis Gkionis (igkionis@eurobank.gr)
(+30) 210 337 1225

Romania: Macro & Market Data			
Macro indicators	**2016**	**2017**	**2018f**
Real GDP (yoy, %)	4.8	7.0	4.5
Inflation (yoy%, avg)	-1.6	1.3	4.5
Fiscal Balance (%GDP, Cash basis)	-2.4	-3.0	-3.5
Gross Public Debt (%GDP, Cash basis)	37.6	36.5	36.1
Unemployment Rate (LFS, %)	5.9	4.9	4.8
Compensation of employees/head	10.3	9.5	6.5
Current Account (% GDP)	-2.2	-3.5	-4.0
Net FDI (EUR bn)	3.9	4.6	4.5
Domestic Credit	**2015**	**2016**	**2017**
Total Credit (%GDP)	43.9	41.2	38.6
Private Sector Credit (yoy)	3.0	1.2	5.6
Loans to Deposits (%)	106.6	114.3	109.2
Financial Markets	**3M**	**6M**	**12M**
Policy Rate (Currently:2.25%)	2.50	2.50	3.00
EUR/RON (Currently:4.66)	4.70	4.70	4.75

Sources: National statistics, Eurostat, IMF, Ecowin Reuters, Eurobank Research

FIGURE 15: Monetary policy & FX rate 2013-2018



Serbia (Ba3/BB/BB)

Real GDP growth to pick up pace this year after supply-side shocks slowdown in 2017

Real GDP growth to pick up pace this year after slowdown in 2017 due to supply-side shocks

Real GDP growth was confirmed at 2.5% in Q4 2017, bringing the full-year rate of increase to 1.9%. The latter compares with expansion of 2.8% in 2016 and is below initial government and market forecasts as adverse weather conditions in H1 2017 weighed heavily on the agriculture and energy sectors. From the supply side showed construction, wholesale and retail trade as well as manufacturing marked the highest growth rates in FY2017. From the expenditure side, recovering private consumption as well as robust investments and exports were the main contributors to economic activity, though the latter's net impact swung into negative on continuously strong imports figures. Economic activity is expected to pick up pace towards 3% this year. Domestic demand is penciled in to remain the key growth contributor. Investments are expected to remain robust, supported by net FDI inflows (at around 5-6% of GDP according to official estimates), amid an improving business environment and low borrowing rates. A further recovery is anticipated in private consumption stemming from higher disposable income amid increasing private sector employment and rises in the minimum salary and public sector wages and pensions. Although exports are seen strong in view of a favorable external backdrop, rising imports via strengthening domestic demand will likely neutralize their positive input on economic activity.

CAD widened last year, but external imbalances significantly improved over the last five years

The increase in the current account deficit, + 95% in 2017 to 5.7% of GDP, is primarily attributed to lower agricultural exports as a result of a bad agricultural season, higher energy imports amid adverse weather conditions and rising oil prices and increasing imports of equipment in reflection of strong FDI inflows. Nonetheless, Serbia's external imbalances have improved in the last years, with the current account deficit having declined from of 11.6% in 2012 remaining fully financed by net FDI inflows since 2015, which reached a 6-year high of EUR 2.4bn or 6.6% of GDP last year.

Inflation pressures remain relatively subdued

Headline CPI slid to a 1-½-year low of 1.5%YoY in February on base effects, having sustainably entered and remained within the 3.0±1.5% target band since late 2016. Confirming still low price pressures, the corresponding core index was just above January's life-time low of 1.2%YoY. Thus, the MPC cut the key policy rate by 25bps to a new 3.25% low in March following stable rates in the prior four meetings. Albeit benign inflationary pressures and the dinar's appreciation recently argue in favor of this reduction, several factors suggest that the monetary easing cycle is close or has reached its bottom. CPI appears to have lately eased on the back of one-off factors and is seen higher later in the year as domestic demand dynamics improve further, labour market conditions remain tight and some fiscal loosening takes place in 2018. Monetary policy normalization by major CBs as well as global oil and food prices also pose risks to the inflation outlook.

SNS victory in Belgrade's local elections in March confirm President Vucic's strong mandate

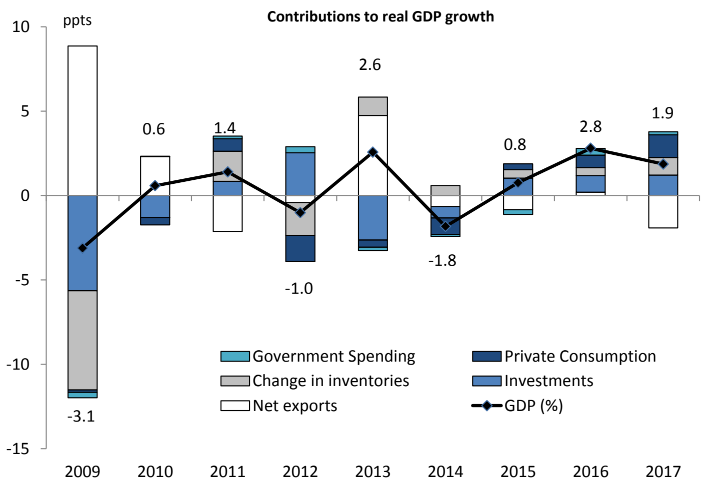
The ruling Serbian Progressive Party (SNS) won 44.99% of the vote in Belgrade's local elections on March 4, claiming 64 seats in the city council. The runner-up, a coalition around former governor of Belgrade Dragan Djilas, won 18.93% of the vote or 26 seats. The polls confirmed that the ruling party still enjoys strong support and additionally strengthen President Aleksandar Vucic's mandate on the domestic political scene. Albeit the said polls were for local offices only, the city's high importance on domestic economics and politics deems it as an indicator of popular support towards political parties.

Galatia Phoka (gphoka@eurobank.gr)
+30 210 3718922

Serbia: Macro & Market Data			
Macro indicators	**2016**	**2017e**	**2018f**
Real GDP (yoy, %)	2.8	1.9	3.0
Inflation (yoy%, avg)	1.2	3.0	3.0
Fiscal Balance (%GDP, Cash basis)	-1.3	1.2	-0.6
Gross Public Debt (%GDP, Cash bas	71.9	61.5	61.0
Unemployment Rate (LFS, %)	15.3	13.5	12.5
Wage growth (total economy)	2.5	0.9	3.2
Current Account (% GDP)	-3.1	-5.7	-4.5
Net FDI (EUR bn)	1.9	2.4	2.0
Domestic Credit	**2015**	**2016**	**2017**
Total Credit (%GDP)	62.3	63.6	60.5
Private Sector Credit (yoy)	3.3	5.6	3.6
Loans to Deposits (%)	99.0	92.0	95.0
Financial Markets	**3M**	**6M**	**12M**
Policy Rate (Current: 3.25%)	3.25	3.25	4.00
EUR/RSD (Current: 118.0)	117.00	115.00	116.50

Sources: National statistics, Eurostat, IMF, Reuters, Eurobank Research

FIGURE 16: Recovery driven by private consumption & investments



Eurobank Economic Analysis and Financial Markets Research

Dr. Tasos Anastasatos: *Group Chief Economist*
tanastasatos@eurobank.gr, + 30 210 33 71 178

Research Team

Anna Dimitriadou: *Economic Analyst*
andimitriadou@eurobank.gr, + 30 210 3718 793

Ioannis Gkionis: *Senior Economist*
igkionis@eurobank.gr + 30 210 33 71 225

Stylianos Gogos: *Economic Analyst*
sgogos@eurobank.gr + 30 210 33 71 226

Olga Kosma: *Research Economist*
okosma@eurobank.gr + 30 210 33 71 227

Mariana Papoutsaki
mpapoutsaki@eurobank.gr + 30 210 33 71 224

Paraskevi Petropoulou: *Senior Economist*
ppetropoulou@eurobank.gr, + 30 210 37 18 991

Galatia Phoka: *Research Economist*
gphoka@eurobank.gr, + 30 210 37 18 922

Theodoros Stamatiou: *Senior Economist*
tstamatiou@eurobank.gr, + 30 210 3371228

Elia Tsiampaou: *Economic Analyst*
etsiampaou@eurobank.gr, +30 210 3371207

Eurobank Ergasias S.A, 8 Othonos Str, 105 57 Athens, tel: +30 210 33 37 000, fax: +30 210 33 37 190, email: Research@eurobank.gr

Eurobank Economic Analysis and Financial Markets Research

More research available at https://www.eurobank.gr/en/group/economic-research

7 Ημέρες Οικονομία: Weekly review of the Greek economy

- **Greece Macro Monitor - Focus Notes:** Periodic publication on the latest economic & market developments in Greece
- **Economy & Markets:** Analysis & research on the Greek and international economy
- **Regional Economics & Market Strategy Monthly**: Monthly edition on economic & market developments in the region
- **Emerging Markets Special Focus Reports:** Periodic publication on specific EM economy and markets developments
- **Daily Overview of Global markets & the SEE Region:** Daily overview of key macro & market developments in Greece, regional economies & global markets
- **Global Macro Themes & Market Implications for the EA Periphery and the CESEE:** Monthly review of the international economy and financial markets
- **Global Markets Special Focus Reports:** Periodic publication on specific global economy and markets developments

Subscribe electronically at https://www.eurobank.gr/el/omilos/oikonomikes-analuseis