

Written By:

Ioannis Gkionis:

Research Economist
Coordinator of Macro Research
igkionis@eurobank.gr

Mihai Patrulescu

Economist
Mihai.Patrulescu@bancpost.ro

Editor:

Platon Monokroussos

Assistant General Manager
Head of Financial Markets
Research
pmonokroussos@eurobank.gr

DISCLAIMER

This report has been issued by EFG Eurobank Ergasias S.A. (Eurobank EFG), and may not be reproduced or publicized in any manner. The information contained and the opinions expressed herein are for informative purposes only and they do not constitute a solicitation to buy or sell any securities or effect any other investment. EFG Eurobank Ergasias S.A. (Eurobank EFG), as well as its directors, officers and employees may perform for their own account, for clients or third party persons, investments concurrent or opposed to the opinions expressed in the report. This report is based on information obtained from sources believed to be reliable and all due diligence has been taken for its process. However, the data have not been verified by EFG Eurobank Ergasias S.A. (Eurobank EFG), and no warranty expressed or implicit is made as to their accuracy, completeness, or timeliness. All opinions and estimates are valid as of the date of the report and remain subject to change without notice. Investment decisions must be made upon investor's individual judgement and based on own information and evaluation of undertaken risk. The investments mentioned or suggested in the report may not be suitable for certain investors depending on their investment objectives and financial condition. The aforesaid brief statements do not describe comprehensively the risks and other significant aspects relating to an investment choice. EFG Eurobank Ergasias S.A. (Eurobank EFG), as well as its directors, officers and employees accept no liability for any loss or damage, direct or indirect, that may occur from the use of this report.

No confidence vote brings down unexpectedly the Romanian government

- **The Romanian government was toppled unexpectedly earlier today by a 4 votes margin, two months after it took office, following a no confidence in Parliament**
- **Political volatility had a negative impact on the domestic financial markets: EUR/RON pair tradrf in a volatile session at levels around 4.39 at the time of writing vs. 4.37 in late hours on April 26**
- **The opposition leader, Mr. Victor Ponta (PSD), is expected to take office as Prime Minister**
- **The risk of fiscal slippage in lieu of the heavy election calendar in 2012 (local elections in June-parliamentary elections in December) is material**

The Romanian government was toppled unexpectedly earlier today, two months after it took office, following a no confidence vote in Parliament. The motion passed with a majority of 235 MPs (4 more than required) from the opposition Social-Liberal Union and last minute defections from the ruling Democratic Liberal Party-**PDL**. Note that the Social-Liberal Union was formed by the national liberal party-**PNL** and Romanian social democrats-**PSD**.

Domestic financial markets reacted negatively on the news, with the EUR/RON pair trading in a volatile session at levels around 4.39 at the time of writing vs. 4.37 in late hours on April 26. Year-to-date, the leu has depreciated by ca 1.5% against the euro on a cumulative basis.

Outgoing Prime Minister, Mihai-Razvan Ungureanu, was unable to fend off defections in the coalition that allowed his predecessor, Emil Boc, to survive 10 such motions in 2010-2011. Mr. Boc resigned on February 6, after violent protests broke out in Bucharest. Emil Boc's government introduced in July 2011 (and consequently implemented) a highly-unpopular fiscal austerity package, consisting of, among other measures: (i) a 25% cut in public-sector wages; (ii) a 5ppt VAT hike to 24%; and (iii) more than 100k lay-offs in the broader public sector.

Social and political pressures to restore public wages have been on the rise lately, especially in view that 2012 constitutes an election year.

President Basescu reiterated on April 25 that the government needs to reverse public wage cuts effectively from June. From his part, the outgoing Prime Minister promised recently that the Cabinet would discuss the issue with the IMF during a regular review of the present programme.

The opposition Social-Liberal Union now holds the majority in Parliament. According to the Romanian constitution, President Basescu (who is in office since 2009 by the support of **PDL**) must nominate a new Prime Minister who will need to gain parliamentary backing. The required procedure could well prove straight forward and swift, although the risk of political acrimony and a tense domestic political environment remains, at least for the short-term. Opposition leader, Victor Ponta (PSD), is expected to take office as Prime Minister.

Romania faces a heavy election calendar in 2012. Local elections are scheduled for June 10 and parliamentary elections for late November. However, if Social-Liberal Union-**USL** forms a new government and also wins the upcoming election, the structure of the new cabinet may not change much after the national ballot.

Romania is currently running a €5bn two-year precautionary arrangement with the IMF and the EU, following expiration of an earlier regular Stand By arrangement in March 2011. The Romanian government has already

completed successfully four reviews under the present programme without making any use of the designated funds so far.

The fifth review of the current programme started on April 24 and was about to finish on May 7. The review has been postponed until the formation of a new government. Talks on a technical level will continue in the background. The leader of the social democrats-**PSD**, Mr. Victor Ponta, has expressed his support to the continuation of the IMF precautionary programme.

Romania has made visible progress in fiscal consolidation in the last couple of years, managing to reduce the general government deficit (on a cash basis) from 7.3%-of-GDP in 2009 to 4.2%-of-GDP year in a highly uncertain domestic economic environment.

Attainment of the current year's fiscal target requires tough austerity measures to remain in place. The outgoing coalition government had targeted a general government deficit of 1.9% of GDP on a cash basis (2.1% including IMF approved off-budget expenditures) in 2012. The budget execution data bring the fiscal deficit at 0.6% of GDP in Q1, in line with the full year target.

Implications for domestic monetary policy: The NBR will hold a regular monetary policy next week (May 2). The bank was broadly expected to cut the reference rate one more time to 5.00%. Provided that the change of government will be swift (our baseline scenario), we believe that the easing cycle will continue, with one more rate easing remaining in the cards in one of the coming policy meetings.

Romanian economy in much better shape now than in the pre-crisis period: Having emerged from an earlier recession, the economy expanded by 2.5% in 2011, for the first time since 2008. Our GDP forecast in 2012 stood at 1% subject to downside risks of Euroarea sovereign crisis. Inflation declined to 3.1%YoY last December, a historical low, coming in well within to the NBR's respective target range (3% +/- 1%YoY). At the same time, the current account deficit ended at 4.2% of GDP far from the unsustainable pre crisis levels.

In conclusion, we will remain watchful as these important events unfold and will keep you informed with the latest developments.

Research Team

Financial Markets Research Division

Platon Monokroussos: *Head of Financial Markets Research Division*

Paraskevi Petropoulou: *G10 Markets Analyst*

Galatia Phoka: *Emerging Markets Analyst*

Sales Team

Nikos Laios, *Head of Sales*

Vassillis Gulbaxiotis, *Head of International Sales*

Yiannis Seimenis, Ioannis Maggel, *Corporate Sales*

Stogioglou Achilleas, *Private Banking Sales*

Alexandra Papathanasiou, *Institutional Sales*

Economic Research & Forecasting Division

Dimitris Malliaropoulos: *Economic Research Advisor*

Tasos Anastasatos: *Senior Economist*

Ioannis Gkionis: *Research Economist*

Vasilis Zarkos: *Economic Analyst*

Stella Kanellopoulou: *Research Economist*

Olga Kosma: *Economic Analyst*

Maria Prandeka: *Economic Analyst*

Theodosios Sampaniotis: *Senior Economic Analyst*

Theodoros Stamatiou: *Research Economist*

Eurobank EFG, 20 Amalias Av & 5 Souri Str, 10557 Athens, tel: +30.210.333.7365, fax: +30.210.333.7687, contact email: Research@eurobank.gr

Eurobank EFG Economic Research

More research editions available at <http://www.eurobank.gr/research>

- **New Europe:** Economics & Strategy Monthly edition on the economies and the markets of New Europe
- **Economy & Markets:** Monthly economic research edition
- **Global Economic & Market Outlook:** Quarterly review of the international economy and financial markets

Subscribe electronically at <http://www.eurobank.gr/research>

Follow us on twitter: http://twitter.com/Eurobank_EFG

